FULL COMMITTEE HEARING ON RAIL TRANSPORTATION ACCESS FOR SMALL BUSINESSES AND FAMILY FARMERS

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FULL COMMITTEE HEARING ON RAIL TRANSPORTATION ACCESS FOR SMALL BUSINESSES AND FAMILY FARMERS

Thursday, May 1, 2008

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The Committee met, pursuant to call, at 10:00 a.m., in Room 1539 Longworth House Office Building, Hon. Nydia Velaquez [chairwoman of the Committee] presiding.

Present: Representatives Velaquez, Grijalva, Cuellar, Altmire, Clarke, Ellsworth, Sestak, Chabot, Bartlett, Akin, and Fallin.

OPENING STATEMENT OF CHAIRWOMAN VELÁZQUEZ

Chairwoman VELAQUEZ. Good morning. I now call this hearing to discuss rail transportation access for small businesses and family farmers.

Small businesses and family farmers in rural America depend on a reliable transportation system to move their goods. In an increasingly global economy, rural companies are just as likely to ship their products across the world as across the country. A key component in helping these businesses achieve success is access to an affordable rail system. Whether exporting wheat to Asia or shipping fertilizer to a small town in Vienna, rural communities have a critical stake in quality rail transportation. In many instances, it is the only option for sending and receiving goods.

Today, we will hear from small businesses and their representatives who have been confronted with both rising rail transportation rates and declining service. The Committee will examine how this problem is affecting entrepreneurs and discuss ways to address it. Most small businesses do not negotiate contracts with Union Pacific. However, they certainly experience the impact of rail rates which have gone up by as much as 80 percent in the last three years.

The rising cost of rail affects nearly all commercial activity in rural areas. Family farmers, in particular, are taking the biggest hit. The payments that wheat and corn growers ultimately receive are directly tied to rail costs. With up to one third of wheat costs attributable to transportation expenses, the situation cannot be ignored. This is especially true when one considers growing concerns of arising food prices.

Rail rates have a ripple effect that extend beyond commodities and throughout the entire rural economy. Local retailers feel the

impact of rising rail transport rates when they purchase fertilizer, seed, and other equipment. When these businesses cannot move and receive their products, it impairs the expansion of the local economy.

Today, increasing costs of rail transportation is also having an enormous impact on affordable energy supplies. Coal is the primary source for electric generation in rural areas and it is shipped across the country on the railways. Unreliable and expensive rail transportation would only lead to higher energy prices.

With small businesses already seeing skyrocketing fuel costs, this transportation problem is creating another major challenge. At a time when there is major focus in rural areas with the development of renewable fuels, there must be infrastructure in place to support this growth. We need to welcome new opportunities for expanding our rural economies and assure valuable shipping options are available at competitive rates.

Clearly, the federal policy framework must be examined to ensure adequate competition. That is especially true when you consider the laws on the books regulating rail transportation were establish at a point in our history when railroads were not financially viable. The nation's rural businesses have shown an ability to adopt and change with the development of new technologies, but to keep their products competitive in the domestic and global markets, transportation is key. In most instances that means rail transportation. If such service is not available at a fair price, American farmers and small businesses will lose market share. Foreign competitors will more easily sell their products to U.S. customers and our rural economy will suffer.

I look forward to hearing about possible reforms to ensure the continued growth of small businesses in rural America. I appreciate the witnesses coming here today and I thank you for taking time off your busy schedule.

I yield to the Ranking Member, Mr. Chabot, for his opening statement.

OPENING STATEMENT OF MR. CHABOT

Mr. CHABOT. Thank you very much, Madam Chair, and thank you for holding this hearing today on rail transportation access for small businesses and family farmers. I also want to thank our witnesses for being here and taking the time out of their busy schedules to share their views with us on this important issue.

Railroads have played a crucial rule in the history and development of our nation and are one of the most important contributors to our economy today. They were critical to the development of the American West, and have had some part in almost all stages of our nation's development. Whether it was shipping steel used to build the Golden Gate Bridge, which was fabricated in New Jersey, or transporting the Indiana limestone and granite which composes the facade of the Empire State Building, railroads have played a key role in creating the face of America and maintaining the health of our economy.

Currently, more than 40 percent of our nation's freight is moved by rail. Many goods Americans depend on and use every day would never even make it into our homes if small businesses and family

farmers could not ship them via rail. For example, coal which is used to produce nearly half of the nation's electricity that lights American homes is shipped by railroads. In 2006, there were 561 freight railroads operating in America with an aggregate revenue of $54 billion.

Railroads, which contribute billions of dollars each year to the economy through wages and purchases, retirement benefits and taxes are vital to keeping America competitive in the world market. Freight railroads employed 186,000 people in 2006 and were one of America's highest paying industries. America's small businesses and family farm depends on the rail system to safely and efficiently ship their goods to the American consumer.

In the past few years, many of these family farmers and small businesses have voiced concern over the rising cost of access to these railroads. It is in the best interest of all Americans that we make sure small businesses and family farmers continue to have access to affordable transport on American rail.

Once again I want to thank Chairwoman Velaquez for holding this hearing and look forward to hearing testimony from all the witnesses here before us this morning and I yield back the balance of my time.

Chairwoman VELAQUEZ. Thank you. It's my pleasure to introduce Mr. David Cleavinger. Mr. Cleavinger is a wheat grower from Wildorado, Texas and currently serves as president of the National Association of Wheat Growers. His production has included wheat, corn, grain, sorghum, seed milo, sorghum silage, corn and sugar beets, along with stock or cattle. NAWG works as a team of state wheat grower organizations to benefit the wheat industry at state and national levels.

Gentlemen, you are welcome, and you will have five minutes for your testimony.

STATEMENT OF MR. DAVID CLEAVINGER, PRESIDENT, NATIONAL ASSOCIATION OF WHEAT GROWERS, WILDORADO, TEXAS

Mr. CLEAVINGER. Madam Chairman and Members of the Committee, my name is David Cleavinger and I am a wheat grower from Wildorado, Texas. I currently serve as the president of the National Association of Wheat Growers and I'm very pleased to be here today to discuss an issue of great importance to the wheat growers that I represent.

Wheat growers know that an effective railroad system is necessary for the success of the wheat industry. By and large, wheat country is centered away from our waterways and ocean ports, leaving us primarily dependent on railroads to move our products to waterway terminals and export facilities.

As the GAO found in a recent study, rates in captive areas can well be above the threshold of reasonableness established under the law and utilized the Surface Transportation Board. Full operating costs to most railroads are about 100 to 140 percent of variable costs. Rates in excess of 180 percent are considered above the threshold of unreasonableness by the STB and are therefore

challengeable. In some captive wheat growing areas the rates have run as high as 300 to 400 percent of variable cost.

Farmers are not in a position to pass their freight costs along to consumers. In fact, we pay freight on fertilizer and other supplies we purchase, and pay freight on the wheat that we ship out. Further complicating our position, these farmers are not the actual customers of the railroads that haul their grain. The grain companies buy the producers' wheat and other grains, and order the freight from the railroad, passing the cost directly to the farmer. This is an important point, because of the rights to appeal to the Surface Transportation Board are granted to the actual rail customers which are the grain companies.

NAWG and other agriculture industry leaders have requested oversight by the Surface Transportation Board, as we believe it is within their charter to do so. But very little progress has been made. The STB's proposed new revisions to simplify guidelines are highly restrictive and would make challenge unreasonable rates virtually impossible for all but a few facilities shipping small volumes of grain. This frustration with a lack of regulatory oversight has led us to help develop and support together with other captive shippers, including the Alliance for Rail Competition, legislation that would strengthen the rules of the game for growers. We believe parts of HR 2125 and Senate Bill 953 would put us in a position to be treated as a customer should be treated.

H.R. 2125 contains language addressing areas of inadequate competition, common carrier obligation, bottlenecks, and terminal access.

It would also develop a system of arbitration of rate and service issues. While we support these bills we also know that these issues will take time to move through the congressional process, so paying heed to the old saying "if you're not at the table, then you are on the menu", we have begun a process of problem resolution with one of the four major Class 1 railroads. Corn, soy, and wheat growers and other interests, along with representatives from BNSF Railways, have formed the Ag Business Rail Council. Our first meeting was in February, and I will have to say we were treated like customers, rather than as a third-party who has been picking up the freight.

The agenda included discussion of railcar allocation, harvest congestion, differential pricing, revenue to variable cost ratios, and what constitutes a "reasonable freight rate." some of these topics will require considerable homework on our part, but we are determined to find solutions for our growers. This is a forum to educate the railroad about the needs of producers. It will also enhance our understanding of the rail freight business, with the ultimate goal of finding mutually beneficial solutions.

Wheat industry leaders have been working on rail rate and service issues for over 30 years. We believe the complexity of this issue has been a deterrent for many of the parties including Congress. It would be easy to throw in the towel and say "we're tired of messing with this", but we can't do that. Opportunities exist to increase service to American agriculture, such as the new STB accountability, HR 2125, and coalitions like the Ag Rail Business Council.

We understand that new railroads are not going to be built, so competition in that sense is unrealistic. What we can accomplish is accountability on all sides, to find good service at reasonable rates.

Madam Chairman, thank you again for allowing me to be here today and I am here to answer any questions that you have.

[The prepared statement of Mr. Cleavinger may be found in the Appendix on page 26.]

Chairwoman VELAQUEZ. Thank you, Mr. Cleavinger.

Our next witness is Dr. Kendell Keith. Dr. Keith is president of the National Grain and Feed Association. He has served for 21 years as NGFA president in charge of the overall direction and has 900 company members in the grain, feed, and processing sectors. The NGFA, founded in 1896, is a broad-based, nonprofit trade association that represents and provides services for grain feed, and grain-related commercial businesses.

Welcome.

STATEMENT OF MR. KENDELL KEITH, PRESIDENT, NATIONAL GRAIN AND FEED ASSOCIATION

Mr. KEITH. Chairwoman Velaquez, Ranking Member Chabot, and Members of the Committee. I am Kendell Keith, president of NGFA. We do have 900 member companies most of which are small businesses throughout the U.S.

One of the paramount concerns for U.S. agriculture and small business in rural communities is that overall rail shipping capacity in the U.S. is not meeting the growth and demand. While the cost of rail service is a matter of concern, more significant is whether there will continue to be predictable service at all in some locations. For that reason, NGFA is supporting legislation that would provide a tax credit for investments in rail infrastructure.

Railroads are rationing rail transport capacity in today's marketplace, often through demarketing strategies that price rail service above economic levels. At the same time, some of the railroads are investing in new infrastructure to serve the growing demand for transportation. But a serious question is will the railroads invest in new infrastructure at the rate that would be desirable by consumers and the customer base of the railroads? We think legislation would help in this regard.

In the grain-based agricultural industry, railroads have been encouraging grain elevators and grain users for a number of years to build the infrastructure to ship longer trains. This also has caused us increasingly concentration of grain handling at fewer loading points which means farmers have fewer points to deliver grain to. So the farm-to-market distance is increasing on average, leading to more traffic on highways and local road systems. The added cost of highway repairs, of course, is borne by the taxpayer.

With the constrained rail capacity, we have seen higher freight rates in grain in the last three years. Revenue per grain rail car has increased between 27 and 52 percent for the major U.S. rail carriers. I might add that that includes both fuel surcharges as well as the rates on the cars themselves.

Part of this rate increase is related to the fuel surcharge issue, but mostly it is tied to increased demand for transportation. We're not judging whether this level of rate change is justifiable or reasonable, but we do think that such rate increases suggest the need to monitor the situation and consider how increasing rail rates may affect rural communities in small business. And the situation of higher rail rates underscores the need to review whether there are effective tools available to shippers to deal with unreasonable rail rates.

The Surface Transportation Board is in the process of making some changes to federal rules that govern the challenge of rail rates. But it's been 13 years since the U.S. Congress passed the Interstate Commerce Commission Termination Act which specifically directed the STB to provide a way for shippers to challenge rates in so-called small rate cases. In that 13 years, no small rate case has been completed which provides ample evidence that the STB for most of that period has been unresponsive to the needs of rail customers in the clear direction given by the U.S. Congress.

There are three cases now pending under STB's new small rate case guidelines. We believe the new STB rules will also prove to be of little use to shippers. This is because the agency chose to cap the potential benefits of such rate challenges at such a low level that it will discourage shippers from bringing cases. We think this approach by the STB will fail to achieve the market discipline on rates intended by Congress and unfortunately also fail to improve the business relationship between railroads and their customer. Thank you again, and we look forward to questions.

[The prepared statement of Dr. Keith may be found in the Appendix on page 35.]

Chairwoman VELAQUEZ. Thank you, Dr. Keith.

Our next witness is Ms. Nelle P. Hotchkiss. Ms. Hotchkiss is Senior Vice President of Corporate Relations for the North Carolina Electric Membership Corporation. She's testifying on behalf of the National Rural Electric Cooperative Association. NRECA was founded in 1942 and is the national organization representing cooperative electric utilities. Welcome.

STATEMENT OF MS. NELLE P. HOTCHKISS, SENIOR VICE PRESIDENT OF CORPORATE RELATIONS, NORTH CAROLINA ELECTRIC MEMBERSHIP CORPORATION, RALEIGH, NORTH CAROLINA, ON BEHALF OF THE NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

Ms. HOTCHKISS. Madame Chairwoman, Ranking Member Cabot, and Members of the Committee: My name is Nelle Hotchkiss and I am the Senior Vice President of Corporate Relations for the North Carolina Electric Membership Corporation. Our membershipconsists of 26 electric cooperatives serving over 2.5 million consumers in 93 counties of the 100 counties in North Carolina. I appreciate the opportunity to speak before you today about the issue of rail transportation and the importance of adequate rail competition in my state and across this nation.

As member-owned, not-for-profit organizations the obligation of rural electric cooperatives is to provide a reliable supply of elec-

tricity to all consumers in our service areas at affordable rates. We take our obligation to serve very seriously. The personal and economic health of our members, our communities, and our nation depends on it.

Electric Cooperatives are dependent on the railroads for the transportation and delivery of coal. Simply put, we do not believe that America's four major railroads are meeting our transportation needs in the most efficient and dependable manner. Electric cooperatives and other rail customers do not receive reliable rail service at reasonablerates. The Surface Transportation Board or STB, the government agency charged with the regulatory responsibility for the nation's railroads, is not addressing crucial rail customer rate and service problems.

Some utilities are being forced to buy more expensive foreign coal because they can't rely on railroad deliveries from the Powder River Basin, the richest source of low sulfur coal in the world.

Electric cooperative consumers in North Carolina and around the country have experienced deteriorating rail service and sharply increased rates. For example, from 2002 to 2007, North Carolina's electric cooperatives experienced a 45 percent increase in the coal freight component of our energy cost which, in turn, was reflected in the wholesale rate of power. That increase calculates to over $8.7 million in higher costs during this time frame than have been borne by our end customers: residents, small farmers, and small businesses. Service problems and high rail costs occur primarily in areas where shippers are captive meaning they have no transportation option but to use a single railroad.

Captive rail customers are shippers who must rely on those single railroads to deliver their products. These customers usually move bulk commodities such as coal, grain or lumber, or certain materials that, due to size or characteristics, cannot be moved on our nation's highways.

Historically, 20 to 30 percent of the nation's rail movements have been "captive", with many of these movements covering rural America. Today, in a capacity-constrained rail system, a majority of rail movements may lack competition.

The nation's antitrust laws are meant to protect consumers and the overall public interest from anti-competitive behavior by businesses. The railroads are exempt from antitrust laws and do not play by the same rules. The railroads' antitrust exemptions are antiquated, have no public policy justification, and allow anticompetitive conduct. The resulting lack of competition, together with ineffectiveness of the STB, have allowed freight railroads to reap huge profits with no market consequences or legal accountability for their unreliable service or exorbitant rates and fees.

There are solutions however. The railroads must be covered by the nation's antitrust laws, just like other industries and the STB must be more responsive to the public interest and concerns of rail customers. Legislative activity in the 110th Congress has moved to give America the railroad system it needs for the 21st century, and to correct current railroad abuses.

Madam Chairwoman, thank you for conducting today's hearing. We look forward to working with this Committee and all other

stakeholders to resolve these critical rail issues in an objective and constructive manner. And I'd be happy to take questions.

[The prepared statement of Ms. Hotchkiss may be found in the Appendix on page 40.]

Chairwoman VELAQUEZ. Thank you, Ms. Hotchkiss.

And now I recognize Mr. Ellsworth for the purpose of introducing our next witness.

Mr. ELLSWORTH. Thank you, Madam Chairwoman. It's an honor for me to introduce one of my constituents from the great State of Indiana. Before I do that though I'd like to take just a second. Mr. Weber and I were talking before the hearing and he inquired about the Farm Bill. Since a lot of farmers and ranchers are small business owners, I think it concerns this Committee that we do pass a Farm Bill. It does come out of conference and the President has signed that. We talk about stimulus packages. If our farmers and ranchers knew what their future held, that might be the stimulus package that we need. So I hope that we can get that out and I'm cautiously optimistic that we have a deal cut and that the President signs that and we can deliver good news to you.

With that, it's my honor to introduce, like I said, a constituent, someone who hails from the great State of Indiana, Mr. Dan Weber. Mr. Weber is chairman of the Agriculture Retailers' Association, otherwise known as ARA. He currently is vice president of agronomy with Ceres Solutions in Terre Haute, Indiana, which is also in my District. The company serves more than a dozen counties with agronomic inputs, energy, grain marketing and a wide variety of other products and services for producers and consumers.

ARA serves agriculture retail and distribution businesses by ensuring a profitable business environment for members.

Mr. Weber, thank you for coming and the floor is yours.

STATEMENT OF MR. DAN WEBER, CHAIRMAN, CERES SOLUTIONS, TERRA HAUTE, IN, ON BEHALF OF THE AGRICULTURAL RETAILERS ASSOCIATION

Mr. WEBER. Thank you for the introduction, Congressman Ellsworth.

Madam Chairwoman and Members of the Committee, thank you for inviting me to testify today on behalf of the Agriculture Retailers Association concerning rail transportation access for small business and family farmers. I'm Dan Weber, Vice President of Agronomy, with Ceres Solutions LLP, a cooperative selling crop inputs and application services in the State of Indiana. I am also Chair of the Board of Directors for the ARA which represents a significant majority of the nation's ag retailers and is located in Washington, D.C.

Ceres Solutions is an agricultural cooperative owned by farmers, operating 26 agronomy retail locations serving 5,000 agricultural producers in Western Indiana with crop inputs and application services. I began my role in the agronomy division of Ceres Solutions in February 2007. My background includes 34 years in agriculture retail sales and management, wholesale fertilizer, crop chemicals and seed distribution in the Midwest Region. Ceres Solu-

tions' key agronomy products marketed to farmers are nitrogen, phosphates and potash.

Rail services played a critical role in the distribution of the necessary crop inputs in the past and was a reasonable cost effective transport alternative. In my job I oversee the procurement and receipt of about 125,000 tons of fertilizer with 40,000 tons of that being rail delivered into our facilities.

In doing business with the railroads for the past three and a half decades, I have experienced a deterioration in the service to the agriculture industry. In the 1960s, the industry moved away from animal manures and bag fertilizer to bulk and spray applied fertilizer. These new fertilizer retail facilities were built next to the railroads. Railroad service to these facilities was acceptable through the '70s, but beginning in the '80s, the railroad began to abandon service to many of the smaller communities and business operations. By the 1990s, most of their service to the smaller communities was lost.

Now, the railroad is giving preference to the unit car receivers. Unless you are a large distribution center fertilizers are typically shipped to your retail operations in small quantities because of the short side tracks and the storage limitations at our retail operations.

As an example, one railroad just announced the rates of the phosphate shipments from Florida which will increase in June by 10 percent for single car shipments while unit train shipment of 65 cars will increase six percent and unit train shipments of 85 or more cars will increase only 3 percent.

An example of excessive fees is the railroad's practice of arbitrarily invoicing for services. If one of our retail locations received less than 25 freight cars per year, we received an invoice of $6,000 for an annual side track connection charge. Most of our facilities in the country average six cars annually.

Furthermore, the railroad has changed their tariffs without giving receivers adequate warning. This practice can result in huge investment losses for our business that have expanded or changed their business model based on the expected tariff or car credits that were in place and we thought would continue. We've learned to get their promises in writing.

One difficulty in dealing with the railroad fees and tariffs is that small business owner has little recourse to challenge the railroad's decisions because of the cost of arbitration and the long length of time the process requires. In my opinion, the railroads increased poor service is caused by: one, the railroads' unwillingness to carry toxic-by-inhalation chemicals which is like our anhydrous ammonia; two, because of their monopoly status on our industry, and third, the lack of oversight by the Surface Transportation Board.

ARA has a number of recommendations in the written testimony, but a few are: increase the transparency in the charges and rates, reform the STB to make it more accountable and responsive and review the railroads' antitrust exemption status.

Please remember that for every rail car that is eliminated, that we receive fertilizer in, we add four semi-trucks to the road to move that same volume.

Thank you, Madam Chairman for allowing me to testify and I will be willing to answer any questions the Committee may have.

[The prepared statement of Mr. Weber may be found in the Appendix on page 47.]

Chairwoman VELAQUEZ. Thank you, Mr. Weber.

Mr. Cleavinger, I would like to address my first question to you. With rising food prices, there has been a great deal of discussion as to what is driving grain and corn prices. Do you believe increasing rail costs are part of the reason we are seeing higher commodity prices?

Mr. CLEAVINGER. No. Rail costs have nothing to do with the price of the commodity paid by on the top side. We've seen a reduction of $4 per bush in wheat in the last two months, yet we haven't seen a reduction in bread costs. So the commodity prices have nothing to do with—on the top side have nothing to do. They have to do with what the farmer actually gets for his wheat, but not what the top side.

Chairwoman VELAQUEZ. Can you explain to us how do rates, rail rates generally affect the bottom line for farmers?

Mr. CLEAVINGER. What we are paid for wheat comes off, the freight cost comes off our per bushel wheat. Like where I am, we take the futures market and subtract the freight costs to get what I'm paid for a bushel of wheat. So that's how an off-rate cost comes off that, including rail, trucking, whatever it takes to get it to the market.

Chairwoman VELAQUEZ. Dr. Keith, I understand you believe that the Surface Transportation Board, STB, is not being proactive in their case management. What are some examples of delivery problems your shippers are facing?

Mr. KEITH. Well, one of the most common complaints we get is when facilities will order a train to be delivered for loading. There are restrictions on how long you have to load. Generally, it's 15 hours or you start to incur penalties. And so you try to plan for the arrival of the train and you try to have labor available, but it is still very unpredictable when some train will be delivered and sometimes they're delivered on Friday night at midnight and those kinds of things, so it forces the labor situation at your facility to be more difficult to manage.

We're also getting some complaints about slow approval of new switches to gain access to rail service, in particular, in new ethanol facilities where they're trying to ship both the ethanol product as well as the DBG's byproduct.

Chairwoman VELAQUEZ. Can you talk to us as to how STB handles those types of complaints?

Mr. KEITH. The STB has a formal complaint process that you have to go through if you want to lay out arguments. They've also got an informal complaint process that you can go to a particular office and sometimes get quick resolution. On things like this, though that have a significant impact on a business, generally, you go through a formal complaint process and those formal complaints can take a long time. That's part of the problem. There was a complaint that was on storage of tank cars that lasted five years from start to finish. And it just shouldn't take that long.

We think the STB is starting to improve in some areas in trying to expedite some, but when it takes five years of litigation, it gets costly. It sours relationships with your carrier and we should be able to do better than that.

Chairwoman VELAQUEZ. Ms. Hotchkiss, one of the problems you mentioned is how the lack of rail car access creates unpredictable or limited coal shipments. Has this problem become so severe that rural electric co-ops are seeking alternatives to coal?

Ms. HOTCHKISS. Madam Chairwoman, this problem—I wish we could do it that quickly or it's like taking off your coat and putting on another coat. When you build a power plant it's built specifically to burn a particular fuel, in this case they're impacted by this problem, our coal plants. So to seek an alternative fuel for those particular plants is really not an option. So what we try to do is when inventories get too low, sometimes we have to buy on-the-spot market which is very expensive and that flows right now to consumers in costs. Or we have to import coal from foreign sources and ultimately it is cheaper to do that which to me just doesn't make sense when we are so rich in that particular mineral resource.

Chairwoman VELAQUEZ. So you don't see in the foreseeable future rural electrical co-ops start shifting towards alternative sources of fuel?

Ms. HOTCHKISS. Well, I think if this particular problem isn't solved, as well as other challenges that we face in the electric industry that perhaps aren't specific to this particular problem, we will be looking at other sources, for instance, natural gas, perhaps. But then you have capacity problems and pipeline issues that they have to be built out for that. So there isn't a really good solution. Our view is that these exorbitant costs and poor service and poor resolution process at the STB needs to be resolved so we can bring a better value to our consumer. Because right now that's not bringing a value to the consumer.

Chairwoman VELAQUEZ. Thank you. Mr. Weber, I heard when you say that you have been involved for almost 34 years or 35 years. Can you compare service and rates from when you began your business with today? What are some of the changes you have seen?

Mr. WEBER. Madam Chairwoman, I think the major change is the shift from the local yard having the control to position our cars versus going to a regional control. The local no longer makes that decision. The cars may be sitting in their yard, but they're taking direction from a regional distribution control.

I think that's the major—before we could talk to the local and tell them what we expected as far as needing a car in so many days or where we were at in movement. Now we don't have—we don't have access to that regional guy, they don't answer the phones. You get recordings instead of people.

Chairwoman VELAQUEZ. With utilization of new technology, is rail service better today than it was 35 years ago?

Mr. WEBER. No. Do you want me to expand on that? I don't think so. I think we have more difficulty getting, specially the two and three-car shipments than we ever have. But I understand the economics. The railroad wants to push for the multiple cars, 65-car plus units, 85 cars. Much more economical for them, but that's not

what our facilities were built around. Most of them were built around two and three car receiving locations in the '60s and '70s and okay it has not improved. It's deteriorated.

Chairwoman VELAQUEZ. Mr. Chabot?

Mr. CHABOT. Thank you, Madam Chair. Mr. Cleavinger, I'll start with you, if I can.

As you had mentioned the rates of reasonableness for shipping have been established by law and are to be used by the STB to evaluate rail rates. The current threshold for the rate of unreasonableness is 180 percent of variable costs. You also stated that some rates in wheat growing areas are as high as 300 to 400 percent above the variable costs. So just a couple of questions. Could you sort of explain what is meant by variable cost, what goes into that and how are shippers in these areas handling the situation right now and how do they make ends meet and what attempts have been made to remedy the situation?

Mr. CLEAVINGER. Well, the AJL Studies were done in 2006, so a lot of this information was from that time period. That's the most recent data we've had. And I stated that some, they have been as high as 300 to 400 percent. With some negotiations we've had with the railroads, they are working. We've had one huge problem in Montana in that state as far as rates go and they are working to get those rates down and I think a lot of it has—is a direct result of our going to the railroads and through this process of bringing legislation forward. Had this legislation not been brought forward, there was no incentive to address rate issues. So all those variable costs are passed on to the producer and also was stated a lot of these efficiency that the railroad has become more efficient with shuttle trains, it has been at the expense of the producer because instead of delivering our wheat to a local facility, we've had to truck it further distances to get to a shuttle facility and putting more costs on producers. So I think that's an important point to make.

The railroad has become more efficient and rates have gone down on shuttle facilities, but it's larger shipments and it has put more costs on the producers.

Mr. CHABOT. Thank you very much. Dr. Keith, if I could go to you next. You had mentioned one of the costs that have to be dealt with is the fuel surcharges which have been going up.

Mr. KEITH. Yes.

Mr. CHABOT. And I assume that that's related to the overall additional increases in energy that consumers are dealing with at the gas pump or that our truckers are dealing with with diesel. It's costing us much more. And my question would be getting to what we, as Congress, or what we as a nation ought to be doing about that, would you agree that one thing, one of the problems is that we're too dependent on foreign sources of energy, we need to go after what we have accessible to us and that two of those places that we do have access to that we've put off limits are up in Alaska and ANWR and in the Outer Continental Shelf. It's a debate we have around here all the time and I don't know if you'd like to weigh into it.

Mr. KEITH. Yes. Dependence on foreign oil is a national problem and we think it's time to get down to business on solving the prob-

lem in practical ways. We don't think that the railroads are out of line by wanting to recoup some of their increased costs. It is the cost of doing business. However, some of the formulas that they had at one stage were extremely biased toward their revenue bottom line and those things, we think have been largely corrected.

We're a little disappointed that the STB did not require the railroads to provide more information about how they compute surcharges across modes because you cannot compare the surcharges applied to grain and compare that whether it's fair compared to coal or intermodal. You simply don't have the data. That was another STB ruling that we were a little disappointed in.

Mr. CHABOT. Thank you. Ms. Hotchkiss, you had mentioned in your written testimony that rail transportation is often unreliable and that this contributes to the loss of customers. In your past experiences what have the railroads done that make them unreliable? Do you have any particular instances?

Ms. HOTCHKISS. What we have experienced nationally is not dissimilar to what the other gentlemen here on this panel have discussed. Time frames that they were supposed to have delivery, we had one instance where a major railroad put an embargo, basically just stopped delivery for a while and there's Catch-22s in that because of certain contractual situations. You can't go to another hauler. And so you're forced perhaps to truck it in and has already been mentioned, if you have to truck it in, you're looking at four or five trucks on the road as opposed to a rail car.

We had tried to meet the railroads in a way of actually paying for the building out of infrastructure when we get into the short line situation. We have paid literally paid for the rail cars. We've tried to get the lighter rail cars that they're asking us and the longer ones for aluminum. So basically, we feel like we keep trying to help and we keep trying to be a good customer and we're not necessarily getting the same response back. And that has just continually been an issue. And so when we run into low inventory situations, we have to find alternative ways to either get the coal there or we have to buy on-the-spot market. We just don't have it. Those are things that wreak havoc on our systems.

Mr. CHABOT. Thank you very much. I should probably note you mentioned Catch-22. I heard this morning on NPR that I believe today is Joseph Heller's—would be his birthday who wrote the book Catch-22 that that comes from. I knew everyone would appreciate me bringing that to their attention.

Finally, Mr. Weber, what type of special handling do the goods that you ship require and are they more difficult to handle and I assume that has something to do with the increased cost as well. Is that correct?

Mr. WEBER. Somewhat. The rail cars they use for coal is the same we use for fertilizer. The same rail cars they use for grain are the same ones we use for fertilizer. They just sweep them out, clean them and they'll load grain going back to the receivers.

The only one that has a special use is the pressurized vessels for anhydrous ammonia. That is a specific use vessel and that adds more cost. The railroad has been asking for a waiver where they wouldn't be held accountable if there was an accident on the rail system and anhydrous was released. They were wanting to cap

their liability there. If they do that, they need to do the same for truckers. We have to employ four more trucks for every rail car we don't receive. Right now, I have real difficulty finding enough trucks when that rail car doesn't show up because there's the difficulty in the drivers—availability of drivers and the NH3 bottles themselves that we need for transport.

Mr. CHABOT. Thank you. And just to make sure I have this clear. The general breakdown would be about—if you had four tractor-trailer trucks, you're talking about the trucks that would equal, in general, one railroad car?

Mr. WEBER. Right.

Mr. CHABOT. Thank you very much. I yield back, Madam Chair.

Chairwoman VELAQUEZ. Mr. Sestak.

Mr. SESTAK. Thank you, Madam Chairwoman. I think I only have three questions. I apologize I wasn't here and if you mentioned this, I hope you don't mind my asking again.

The question I have is mainline railroads began to rent out or do other short line railroads. There were certain agreements made, you might say certain restrictions at times made to what's known as you well know, paper barriers. What is your take, if I might ask, you two gentlemen, about this impact for—on rail-to-rail competition in the sense that—I mean should there be some movement towards disallowing these to help this ability to bring down price?

Mr. CLEAVINGER. Obviously, if there's an agreement that only one railroad can carry freight and they have to carry that freight and other competition is not allowed, it affects what cost will be involved in that freight carrier. So those paper barriers of allowing only that short line to carry that freight causes anti-competition.

Mr. KEITH. Our view is that sometimes paper barriers are necessary on a temporary basis, maybe for a three or five-year period because it affects the value of the line. And the railroad may be faced with situations do we abandon the line or do we spin it off and if they spin it off and it's affordable to operate for a short line operator, then we think there may be some justification for a short period of time. But maybe the burden of proof should shift. If you've got one of these and it extends beyond say five years, the burden of proof should be on the carrier to demonstrate why it's necessary to have an agreement like that in perpetuity.

Mr. SESTAK. So you're saying after a while it may be bad public policy to not allow shippers to utilize all potential routing options?

Mr. KEITH. Yes, and to the extent you can create competition by forcing—

Mr. SESTAK. Is this something STB should look at?

Mr. KEITH. They already have looked at that.

Mr. SESTAK. Have they looked at it well?

Mr. KEITH. My conclusion is the way the STB decided on this was that they decided not to establish any firmer rules or guidelines than what exist today.

Mr. SESTAK. Got it. Let me ask that question along the same line, if you don't mind, bottlenecks, through rates. Has that also had a similar impact upon the cost so that somebody ships from Washington, D.C., Chicago, but it goes to Pittsburgh and so you could off-load or short line or something there, but you do not ever see that they are permitted only to show you what the through rate

is rather than showing you what the competitor might do here. There's this—would that help at all?

You know what I'm talking about.

Mr. KEITH. There's no question that competition affects rates.

Mr. SESTAK. But is this a problem, this bottleneck through rate issue on the cost again, it's something we should be looking at?

Mr. KEITH. It's probably more of a problem in the energy than it is in agriculture per se, but yes, there's places where it does create issues.

Mr. SESTAK. Ms. Hotchkiss, did you have a comment on that, since you mentioned energy?

Ms. HOTCHKISS. Yes, sir. Bottleneck rule has been a problem. One particular cooperative in Arkansas had experienced this and a third-party independent carrier was willing to do it and they could not and it does increase the cost. There's no doubt about it.

Mr. SESTAK. Are they precluded from it or are they self-precluded from it because they know somebody else will—they could be two main lines doing this, but one main line from Pittsburgh, he may have—from Chicago, but he knows that if he offers a separate rate, he's going to be jammed on the other side. Is that wrong?

Ms. HOTCHKISS. No. I mean I think there are times when there may be a situation that does exist and needs to be addressed, but I think there have been abuses using this.

Mr. SESTAK. Is this something STB should look at?

Ms. HOTCHKISS. Absolutely.

Mr. SESTAK. Do they do it well now?

Ms. HOTCHKISS. The ruling so far have not been in favor of the shippers.

Mr. SESTAK. My last question is probably more philosophical, but the common carrier obligation under Title 49, what do you believe is reasonable obligation? Has the STB interpreted that correctly, do you think under Title 49 to provide real services at a reasonable request of obligation? Do you know what I'm asking, sir?

That's kind of a subjective phrase.

Mr. KEITH. We are concerned because we've got capacity limits today and because we're not seeing an expansion of capacity in rail that we're going to run into more and more service problems dealing with this issue. I think the issue, in particular, though may be a sensitive one for the chemical industry.

Mr. SESTAK. Is that?

Mr. KEITH. The chemical industry in situations where the railroads would like to see some relief from the common carrier obligation because of what they perceive as the risk involved in hauling that type of freight, but that's really not in my area of expertise.

Mr. SESTAK. I guess and this is something—I'm done for time. I'm sorry.

Chairwoman VELAQUEZ. Time has expired.

Mr. Bartlett.

Mr. BARTLETT. Thank you very much. Two of the reasons that your costs are going up are lack of competition and the increase in energy costs. It's very attractive when looking at the increasing energy costs to question why we haven't drilled in ANWR and offshore and on our public lands. I for one am glad that we have not drilled there because I have 10 kids and 16 grandkids and 2 great

grandkids and I'd like to have a little energy for their generation, thank you.

The world has now reached its maximum capability for producing oil. That happened in our country in 1970. It has happened in the world now. IEA and AEA, the two big organizations that track this have verified that with their data. There's a finite amount of oil in the world. It is not infinite. If we drilled ANWR it would be ten years before any of that hit the market. It is not a solution to our current problem. I'd just like to get that on the record, Madam Chairman. There are solutions to our current problem. Drilling in ANWR or offshore or public lands is not one of those solutions.

Your rates are up for shipping. Are the railroad companies making exorbitant profits?

I haven't seen their profit sheets, but I would doubt that they're making exorbitant profits. So we have to look at why the rates are up. Is their cost shifting? Are some of their customers getting lower rates and they are disadvantaging you by increasing your rates?

Before we know how to solve a problem, we have to know what the problem is. I don't really know what the problem—you have a problem and that is unreliable service and rates that are too high. But I don't know why the service is unreliable and why the rates are too high. Clearly, lack of competition and Mr. Cleavinger, I was very interested in your first graph. It looked like a tennis elimination. We start out with a whole lot of railroads and now we're down to four. Country-wide, we're now down to four railroads.

Madam Chair, I don't know what the ultimate solution is, but clearly, clearly, we have got to have competition. Unfortunately, we have been moving away from rail to trucks which are just a little handier and when oil was $10 a barrel and I remember buying gasoline six gallons for a dollar, six gallons for a dollar back during the Depression. I can remember that. It didn't make any difference that it was five times more expensive than moving by truck than it was by rail because it was so darn cheap to move it either way because energy was so cheap. That's not true today. And unfortunately, we have allowed our rail system to deteriorate. We have had a Rails to Trails program. I'm glad for that, as I mentioned, when I said hello to you because now that means those road beds are still there and now in the future, Madam Chair, we may have a very aggressive Trails to Rails program, as we take those roadbeds and put rails back on them.

I don't know what the problem is and until we know what the problem is we don't really know how to get a solution. You have a problem. That is your rates are too high and your service is unreliable and I think it's incumbent on us to try and find out why and what can be done about it, to turn back the hands of time and to start over and to keep in place the enormous rail system that we have. Now unfortunately, we have developed an infrastructure in our country which is essentially unsustainable in a carbon-deficient world. We have nowhere near the rail transportation that Europe has, for instance, and the developing countries are now putting in rail transportation because that's their first transportation.

So I am very interested in this hearing. Thank you, Madam Chairman for holding it. I just don't know what the problem is.

And until I know what the problem is, I don't know how to address the problem.

I thank you all very much for your testimony. We appreciate, for the record if you can, your analysis of what you think the problem is and how we can solve these problems. If they're cost shifting, we need to stop that. If someone else is getting good service and you're getting lousy service because of discrimination against you, we can help stop that. But we don't know what the problem is and until we know, we don't know how to solve the problem.

So thank you very much for your input and Madam Chair, thank you for holding this hearing and I yield back.

Chairwoman VELAQUEZ. Ms. Fallin, are you ready? If not, I could go on and ask some questions. Are you ready to ask your questions now?

Ms. FALLIN. I might just ask a few. Thank you. I wish I could have made it to your testimony a little earlier, but I had some other commitments, but I appreciate all of you being here today. In my State of Oklahoma much of our state was built with railroads throughout our rural communities and were very important to the beginnings of our state and of course, now as has been mentioned, we're seeing a decline in access and available and infrastructure. I also serve on the Transportation Committee, and so we talk about rail a lot and all modes of transportation for our nation. And as was mentioned by Congressman Bartlett, we are experiencing some challenges with our energy industry and how do we supply the energy that our nation needs and the world needs. I can disagree with him though on the need to look at other energy sources and more exploration of production. I hope we do do that as a nation.

And as we continue to look at alternative sources of fuel, are there any other alternative sources of fuel that can be used in the rail industry that maybe Congress could help encourage? I know that your main source of energy on the rails are usually coal. That may not be in your expertise, but do you see any other forms of energy that could be used to power the rail systems and help you transport your goods and services?

Ms. HOTCHKISS. As the energy person here, I don't know that I could address specifically to provide an alternative fuel to the actual railroad itself. I will tell you they also move material that we use for the operation of our nuclear plants. And to provide—these are base load plants. These provide power 24-7 and rail is very important in that aspect, so to switch to different types of fuels for us away from more conventional fuel which we use for base load at this time with the technology that we have today, we are still going to be dependent on the rails for quite some time.

I'd like to take a moment to address something that Mr. Bartlett said is that we would love to see more transparency with the STB, to find out why some of these costs are so high. So I absolutely agree with you, sir. I think that is part of the concern that we have. We have these decisions come down and we're not exactly sure why they made that decision and typically they're not helpful to us. But you'd have to ask the railroads as far as alternatives to be able to literally move the trains down the track. I don't know enough about that industry to tell you.

Mr. KEITH. Diesel is the primary fuel for locomotives, but there has been some technological gains in diesel fuel utilization and I mean the engines that they're making today are much more efficient than they were say ten years ago. And so as we try to expand capacity, the addition of new locomotives will help the fuel efficiency.

Today, with current technology, there's really not a good replacement for diesel, at least at this stage. There are concepts in development, but it's probably going to be diesel for quite a while.

Ms. FALLIN. I was meeting with a railroad concern a couple of weeks ago and they were talking about the cost mile per gallon in transporting of services and goods on trucking versus the railroad and we're saying when you look at the miles per gallon per transport that the rails actually have a better cost factor when it comes to delivering products and services versus the diesel engine of a truck. And I don't know if you've ever—of course, you may not be able—I don't know if your industries can use trucking at all, but I'm sorry I missed all your testimony, but have you ever looked at the cost comparison between shipping on rails versus shipping on the road?

Mr. WEBER. We receive probably the 125,000 ton. We use 40,000 ton by rail and the rest is by truck. And we—the cost to do the trucking for us is more of a time issue. We can get more timely delivery with a truck. Rail is still the cheapest delivery because our product comes from the phosphate mines in Florida, the Canadian potash mines and then we have four nitrogen producers left in the United States and one large one in Canada. All of our product travels long distance. We bring the product primarily to a central hub distribution center. Then we have to truck it out of there if we cannot receive direct distribution by rail from the production. And so, yes, we use trucks and it is more expensive for us, but it sometime is the only way we can put product into our ag retail facilities.

Ms. FALLIN. Is that because of availability of rail or is it sometimes based upon congestion, like we talk a lot about congestions on our highways and how congestion is time and it's money when it comes to shipping products and goods.

Mr. WEBER. I would say that in listening to the railroad systems and some of their comments, congestion is an issue because so much more product is moved by rail than it was ten years ago. It is much more economical for them to ship a 65 or an 85-car unit to an area and then allow us to truck it rather than to continue as we have had in the past with a two- and three-car receivers. The two- and three-car receivers is still my cheapest way of receiving product. From an economic and a rail congestion perspective, they are doing the things that are going to make them the most money and that is the unit trains. But that is not what we have invested in from our ag retail facilities since the 1960s. We were building these facilities on two- and three-car receiver locations.

Ms. FALLIN. Thank you so much. I think it takes a combination of both, rail and trucking to make it all work.

Mr. WEBER. It is now, yes. I agree with you.

Ms. FALLIN. Thank you.

Chairwoman VELAQUEZ. Dr. Keith, as demand for rail transportation grows, our rail shipping network will continue becoming strained, creating capacity constraints.

From your experience what is the best way to address the issue of limited rail capacity?

Mr. KEITH. Well, to the extent that you can, we think you should rely on the industry, private industry making decisions as to where we need capacity most. If you look at railroad where capacity constraints exist, it's not even throughout the system and the railroads really know best where their constraints are most serious and need to be dealt with.

We support this concept of an investment tax credit, at least on a limit basis because we think it would speed the investment decisions. We think we would get more bang for the buck early on in the process and we're quite fearful that if start to get another growth spurt in this national economy that we're going to see constraints like we've never seen before if we don't build infrastructure soon.

Chairwoman VELAQUEZ. To expand rail capacity, do you think that only by investment and commitment coming from railroads or do you think that a combination of the federal government and the private sector?

Mr. KEITH. We think the federal government has some involvement and some responsibility, frankly, from a national network for transportation. The federal government doesn't want to have to build more and more highways because we've run out of rail capacity and pushed freight on to highways. And so there's a national interest here, we think, but we also think we need a system of monitoring how those investments were made and to make sure that we are expanding capacity and we're not just replacing old ties and infrastructure. We need new capacity.

Chairwoman VELAQUEZ. Any other of the witnesses would like to comment?

You all agree on this? Okay.

Ms. Hotchkiss, you discuss the problems that small shippers face in the agriculture industry and you discuss the lack of transparency of STB. Do you think that within the authority that was granted to STB that they can make the changes or do you believe that a legislative fix is needed, and if it's needed, what are the legislative options that are before us, which one addresses the issues that you raise?

Ms. HOTCHKISS. Well, thank you, Madam Chairwoman for that question. We have—I would agree with Dr. Keith that the STB is working on things. Our concern is that it perhaps won't go far enough or that perhaps these conversations are going on the Hill that that conversation now is taking place at STB.

Our particular thought in what would make our consumers, I think, more comfortable and our customers more comfortable would be that Congress look at reforming the STB. Chairman Oberstar has Bill 2125 and that would make STB more accessible to rail customers.

One of the things I wanted to bring to light, especially for small business, to go through the formal process. It can cost $175,000 just to file a case. That doesn't include the money that goes—it

goes into the millions of dollars to actually see that case through when we're looking at two and three and four and five years of working on one issue. So we do believe that legislative and reform legislation is necessary.

There is also the Antitrust Enforcement Act, HR 1650. That was reported out of House Judiciary yesterday and we are supportive of that legislation as well. When the Staggers Act was changed in 1980, this was a problem that antitrust exemptions continued and I think it can help address some of the issues we've talked about today.

Chairwoman VELAQUEZ. Any other of the witnesses would like to comment on any legislative fix to the problems facing?

Mr. CLEAVINGER. We just believe if the STB is accountable and fixes some of these problems that we've seen and actual accountability on their end and rate cases, as Ms. Hotchkiss said, they're very expensive to file and they haven't been very effective up to this date, so if we would require STB to be more accountable we feel like that would be part—help part of the problem.

Chairwoman VELAQUEZ. Thank you. Mr. Chabot, do you have any other questions?

Mr. CHABOT. Yes, more a comment than a question. Unfortunately, the gentleman that I wanted to respond to had left the room, but I'll be brief and I was going to be kind in any event, but relative to whether or not we should go after the energy that is contained in ANWR up in Alaska or in the Outer Continental Shelf, the—excuse me, the gentlemen mentioned what well, even if we passed it now, we wouldn't get it for ten years or some—that's what he said, but we don't know the exact number. It would be a number of years down the road until we actually got it. This legislation has been before this Congress for over the last ten years and unfortunately, the Congress has decided to keep that off limits. So had we voted this way—Bill Clinton vetoed legislation when it went to his desk some years ago that would have included ANWR, so had we done it back then we'd have the access to that oil now so that would be reflected in the amount that we have available to us here and would be reflected in the energy costs that we're paying and the gas that we're paying at the gas pumps.

And also, I would note that even if we—since we didn't take that action back then and I argue we should have, even if we did take the action now, much of the price reflected at the gas pumps that's killing consumers in this country right now is speculative in nature. So if we pass this now, I think you would see that reflected very quickly even though we wouldn't necessarily get the oil to them now because what happens out there is people are betting on what it's going to be down the road, and right now people think it's going to be higher and higher. And if we continue to put large amounts of our oil that we know about off limits, ANWR, Outer Continental Shelf, it's going to continue to go up and there are other things that we need to do as well, like make it possible to build oil refineries, once again in this country. We've made that virtually impossible. The last one we built is back in '76.

We had over 300 oil refineries in this country at that time. Now we have fewer than half that. We have 148. So even if we have enough crude, we can't refine it quickly enough. These boutique

fuels that have to be dealt with makes it that much more difficult to solve this problem. And I am very much for what many of my colleagues on the other side of the aisle would also be for and that's alternative sources of energy, whether it's wind, solar, biomass, all those, hydrogen fuel cells. We do need to put money into those technological advances somewhere down the road. But until those occur, the fact is we in this country, as other countries around the world, we're very dependent upon gas and diesel and the rest, and unless we do something about it, we're going to have some real problems.

And that, I think, is reflected in the weakness of the economy to some degree and whether we're in a recession and we argue about that all the time, whether we're in a recession, apparently 81 percent of the American people, according to some poll I saw recently, think we are in one, and of course, it depends on the definition. The definition that's accepted is two quarters of negative economic growth and one just came out indicating that it was low growth, but it wasn't negative. So apparently, by definition, we're not in a recession, but whether we are or whether we're not, it's tough times out there for a lot of people. One thing that we could do to help is at the gas pump and that's why I'm so supportive of going after what we have ought to have gone after a long time ago and that's ANWR and the Outer Continental Shelf.

Does anybody want to comment? You don't have to. Okay, thank you very much, and I yield back.

Chairwoman VELAQUEZ. Ms. Fallin?

Ms. FALLIN. Amen.

Mr. CHABOT. Let the record reflect that the gentle lady from Oklahoma said amend.

Chairwoman VELAQUEZ. Let me just say that we will continue to monitor this issue and look at what the Transportation Committee is doing regarding Mr. Oberstar's legislation. One possibility might be to bring some of the railroad executives here and STB to answer some of the concerns that have been raised here.

With that I ask for unanimous consent that Members will have five days to submit a statement and supporting materials for the record. Without objection, so ordered. This hearing is now adjourned.

Thank you.

[Whereupon, at 11:18 a.m., the hearing was concluded.]

NYDIA M. VELÁZQUEZ, NEW YORK
CHAIRWOMAN

STEVE CHABOT, OHIO
RANKING MEMBER

Congress of the United States
U.S. House of Representatives
Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515–0515

STATEMENT
of the
Honorable Nydia M. Velázquez, Chairwoman
House Committee on Small Business
Hearing on:
"Rail Transportation Access for Small Businesses and Family Farmers"

May 1, 2008

Small businesses and family farmers in rural America depend on a reliable transportation system to move their goods. In an increasingly global economy, rural companies are just as likely to ship their products across the world as across the country. A key component in helping these businesses achieve success is access to an affordable rail system.

Whether exporting wheat to Asia or shipping fertilizer to a small town in Indiana, rural communities have a critical stake in quality rail transportation. In many instances, it is their only option for sending and receiving goods.

Today, we will hear from small businesses and their representatives—who have been confronted with both rising rail transportation rates, and declining service. The Committee will examine how this problem is affecting entrepreneurs, and discuss ways to address it.

Most small businesses do not negotiate contracts with Union Pacific. However, they certainly experience the impact of rail rates, which have gone up by as much as 80% in the last three years.

The rising cost of rail affects nearly all commercial activity in rural areas. Family farmers, in particular, are taking the biggest hit. The payments that wheat and corn growers ultimately receive are directly tied to rail costs. With up to one-third of wheat costs attributable to transportation expenses, the situation cannot be ignored. This is especially true when one considers growing concerns over rising food prices.

Rail rates have a ripple effect that extends beyond commodities and throughout the entire rural economy. Local retailers feel the impact of rising rail transport rates when they purchase fertilizer, seed and other equipment. When these businesses cannot move and receive their products, it impairs the expansion of the local economy.

Today, increasing costs of rail transportation is also having an enormous impact on affordable energy supplies. Coal is the primary source for electric generation in rural areas, and it is shipped across the country on the railways. Unreliable and expensive rail transportation will only lead to higher energy prices. With small businesses already seeing skyrocketing fuel costs, this transportation problem is creating another major challenge.

At a time when there is major progress in rural areas with the development of renewable fuels, there must be infrastructure in place to support this growth. We need to welcome new opportunities for expanding our rural economies, and assure viable shipping options are available at competitive rates.

Clearly, the federal policy framework must be examined to ensure adequate competition. That is especially true when you consider the laws on the books regulating rail transportation were established at a point in our history when railroads were not financially viable.

The nation's rural businesses have shown an ability to adapt and change with the development of new technologies. But to keep their products competitive in the domestic and global markets, transportation is key. In most instances, that means rail transportation.

If such service is not available at a fair price, American farmers and small businesses will lose market share. Foreign competitors will more easily sell their products to U.S. consumers, and our rural economy will suffer.

I look forward to hearing about possible reforms to ensure the continued growth of small business in rural America.

U.S. House of Representatives
SMALL BUSINESS COMMITTEE
Representative Steve Chabot, Republican Leader

Thursday, May 1, 2008

Opening Statement of Ranking Member Steve Chabot

Rail Transportation Access for Small Businesses and Family Farmers

I thank the Chairwoman for holding this hearing today on Rail Transportation Access for Small Businesses and Family Farmers. I also thank our witnesses for being here and taking time out of their busy schedules to provide us with their views on this important issue.

Railroads have played a crucial role in the history and development of our nation and are one of the most important contributors to our economy today. They were critical to the development of the American West and have had some part in almost all stages of Our Nation's development. Whether is was shipping the steel used to build the Golden Gate Bridge, which was fabricated in New Jersey, or transporting the Indiana limestone and granite which composes the façade of the Empire State Building, railroads have played a key role in creating the face of America and maintaining the health of our economy.

Currently, more than forty percent of our nation's freight is moved by rail. Many goods Americans depend on and use every day would never even make it into our homes if small businesses and family farmers could not ship them via rail. For example, coal, which is used to produce nearly half of the nation's electricity that lights American homes, is shipped by railroads. In 2006, there were 561 freight railroads operating in America with an aggregate revenue of $54 billion. Railroads, which contribute billions of dollars each year to the economy through wages, purchases, retirement benefits and taxes, are vital to keeping America competitive in the world market. Freight railroads employed 186,000 people in 2006 and were one of America's highest paying industries.

America's small businesses and family farms depend on the rail system to safely and efficiently ship their goods to the American consumer. In the past few years, many of these family farmers and small businesses have voiced concern over rising cost of access, to railroads. It is in the best interest of all Americans that we make sure small businesses and family farmers continue to have access to transport on American rail.

Once again, I thank the Chairwoman for holding this hearing, and look forward to hearing testimony from all of the witnesses.

Statement of Rep. Jason Altmire
Committee on Small Business Hearing
"Rail Transportation Access for Small Businesses and Family Farmers"
May 1, 2008

Thank you, Madam Chair, for holding today's hearing to discuss rail transportation access for small businesses and family farmers. Small businesses across the country rely on dependable transportation to move their goods across the country, and increasingly, around the world. Access to an affordable rail system is key in helping our small businesses achieve economic success. According to the testimony provided, small businesses have found themselves confronted with the challenge of rising rail transportation rates.

In some cases, rail transportation rates have gone up by as much as 80 percent in the last three years. This rising cost affects nearly all aspects of commercial activity. One example is in the cost of wheat. One third of wheat costs are attributable to transportation expenses which is contributing to the rising price of many other consumables.

Our nation's small businesses have shown the ability to change and adapt with the emergence of new technologies that transform the way they operate. To keep them competitive in the domestic and global markets, transportation is key. I look forward to hearing from our panel of witnesses and to discuss ways we can help them with the challenges that they face.

Madam Chair, thank you again for holding this important hearing today. I yield back the balance of my time.

# # #

National Association of Wheat Growers
415 Second St. NE, Suite 300 • Washington, DC 20002 • (202) 547-7800 • www.wheatworld.org

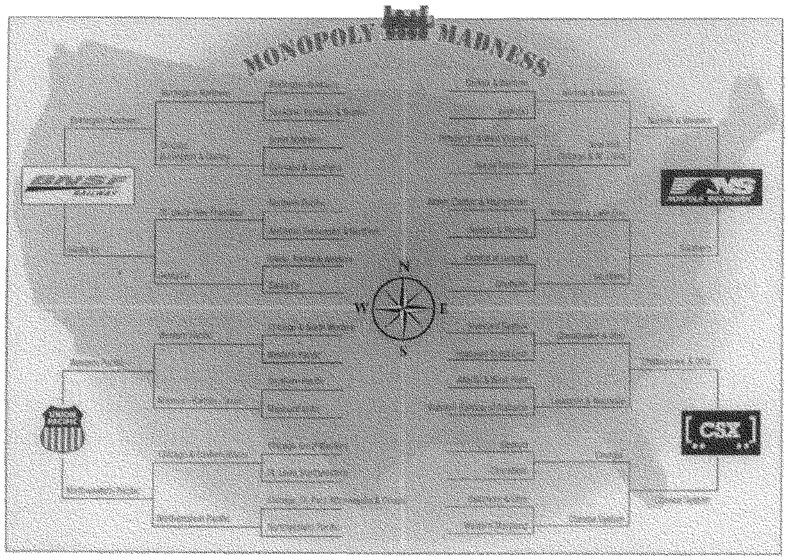
Testimony of David Cleavinger
President
National Association of Wheat Growers
Before the House Committee on Small Business
Hearing to review rail competition and service
May, 1 2008

Madam Chairman and members of the Committee, my name is David Cleavinger. I am a wheat grower from Wildorado, Texas, and I currently serve as president of the National Association of Wheat Growers (NAWG). I am very pleased to be here today to discuss an issue of great importance to the wheat growers that I represent.

Wheat growers know that an effective railroad system is necessary for the success of the wheat industry. And while growers are committed to seeing an effective transportation system at work, over time, agriculture producers in the United States continue to suffer problems with rates and service. Helping our members find solutions to rail freight problems remains one of NAWG's top priorities.

There has been a lot of rhetoric in the past decade about the global economy, but wheat producers have been selling their product into a predominantly world market for over sixty years. Wheat is not typically used locally, therefore it endures long-distance transportation. By and large, wheat country is centered away from our waterways and ocean ports, leaving us primarily dependent on railroads to move our product to export facilities. Many times and in many locations, an ever-consolidating rail system has taken advantage of our dependence and lack of transportation options.

In 1980, we had over 40 Class I railroads serving this nation. In the convention of March madness, here is a graphic depiction of the massive concentration that has occurred over the last 25 years which left us with the final four!

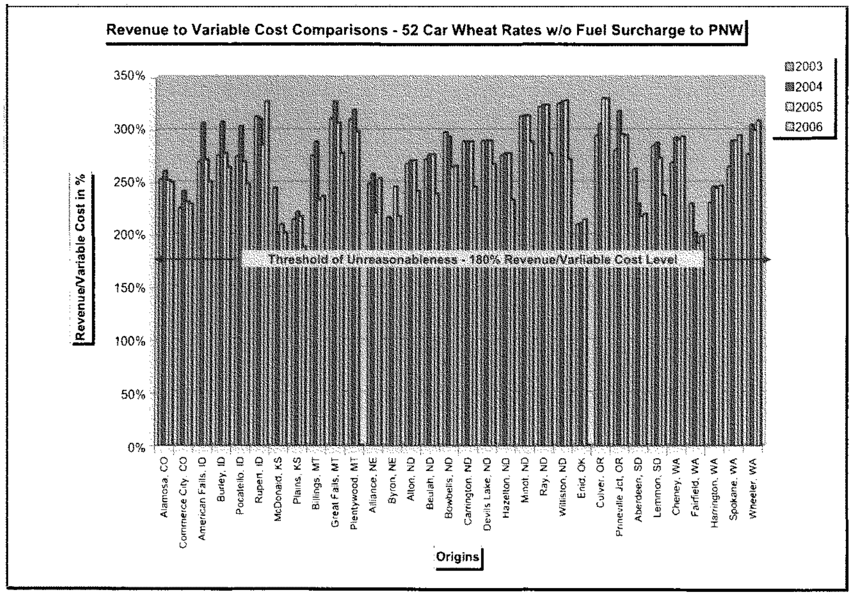


It's the opposite of competition. In 1980 there were over 40 railroads. Today there are just four major railroads that have divided the country into their own regional monopolies. Congress needs to stop the Monopoly Madness by reforming the Surface Transportation Board. Because when railroads compete, consumers win.

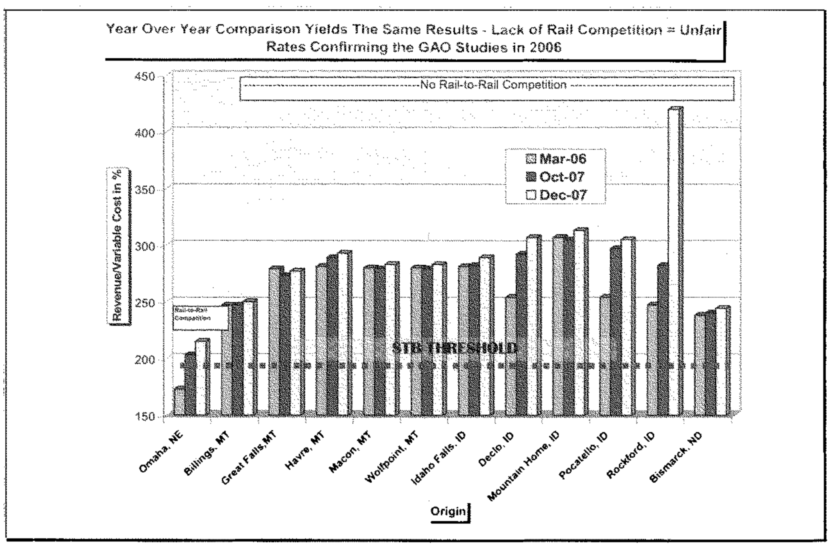
Today, four major Class I railroads serve the United States controlling over 94 percent of the ton-miles, with two of these, the Union Pacific and the BNSF Railway, serving our primary wheat production west of the Mississippi River. While short line railroads may fill gaps in some areas they are tied to their Class I's under what are known as "paper barriers," which restrict their ability to act independently. Thus there are regions with little or no rail competition whatsoever. Where monopolies rule, our wheat growers believe effective oversight of rates and service is needed.

Rates and service issues

As the Government Accountability Office found in a study completed in 2006, rates in captive areas are well above the threshold of reasonableness established under the law and utilized by the Surface Transportation Board (STB). (For explanation of what Rail costing is and how it is interpreted, please see the "Rail Cost Primer" attached at the end of my testimony.) Full operating costs to most railroads are about 130-140 percent of variable costs. Rates in excess 180 percent are considered above the threshold of unreasonableness by the STB and are therefore challengeable. In some captive wheat growing areas the rates can run as high as 300 to 400 percent or more of variable cost.



Provided by Whiteside and Associates, 3203 Third Avenue North Suite 301, Billings, Montana 59101



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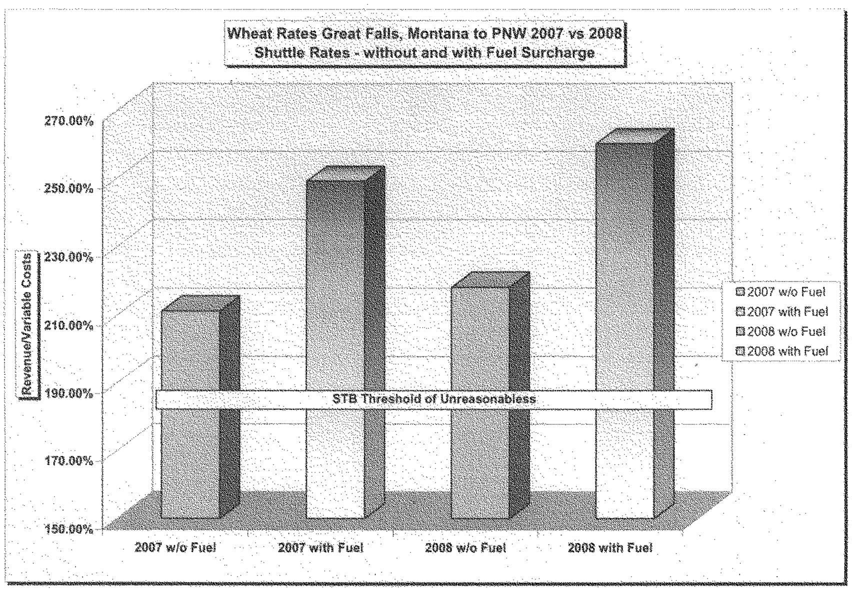

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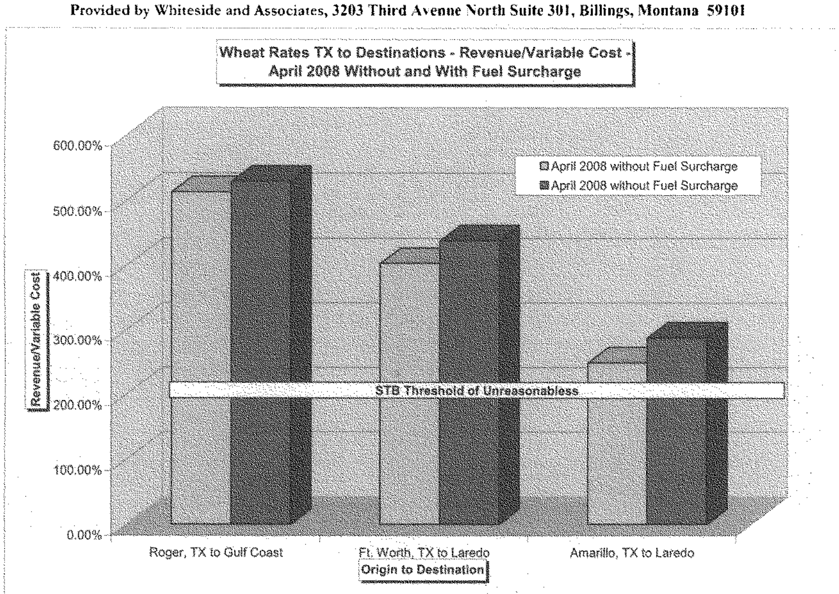
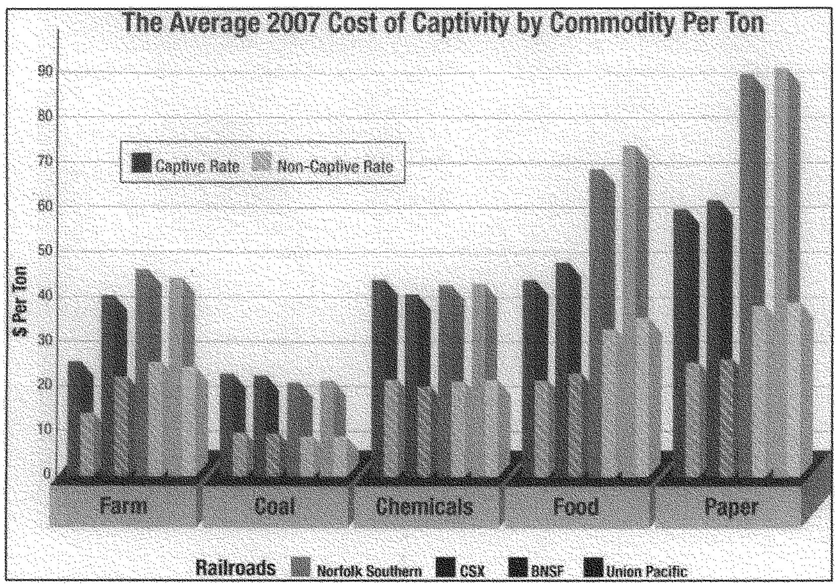


Provided by Whiteside and Associates, 3203 Third Avenue North Suite 301, Billings, Montana 59101

The areas of rail captivity that result in high freight rate levels include parts of Colorado, Idaho, Kansas, Minnesota, Montana, Nebraska, North Dakota, Oklahoma, Oregon, South Dakota, Texas and Washington.

Escalation Consultants, a Washington, D.C. based firm, recently completed studies of the cost of captivity by industry based upon 2007 figures. The chart below clearly shows that the cost of captivity is being borne by most customers.



Escalation Consultants, http://www.escalationconsultants.com/

While service in many areas seems to be getting better, there were pockets in 2007 that suffered from lack of adequate service. In the fall of 2007 for example, over 10 million bushels of grain had to be stored on the ground in Colorado because of the lack of rail service. Storing grain on the ground diminishes value and causes market delivery disruptions. Efforts by Colorado's Governor to provide emergency orders on trucking to facilitate movement from grain piles to railheads outside of Colorado proved to be only marginally successful.

Shifting costs

One of the more difficult problems for growers is that costs are shifting to them as railroads increase their efficiency. While fewer, larger grain elevators decrease railroad costs and speed movement of grain to our ports; farmers are required to truck their grain ever increasing distances to more distant and fewer elevators. While these shuttle facilities may offer higher prices (lower freight rates), there is an increased cost to the grain producer to relocate their

grain to the shuttle. States are also seeing increases in maintenance costs in both primary and secondary highways due to the creation of the shuttle system. Grain producers are not opposed to increasing the efficiency of the grain handling system, but the costs are being borne by the farm producers and the grain industry.

Farmers are not in a position to pass their freight costs along to consumers. In fact, they pay freight on fertilizer and other supplies they purchase, and pay freight on the wheat they ship. Further complicating their position, these farmers are not the actual customers of the railroads that haul their grain. The grain companies, which buy the producers' wheat and other grains, order the freight from the railroad, and then pass the cost directly to the farmer. This is an important point, because most of the rights of rate and service appeal to the Surface Transportation Board are granted to the actual rail customer - the grain companies.

Working for a solution

NAWG and other agriculture industry leaders have requested oversight by the STB, as we believe it is within their charter to do so. Very little progress has been made. The STB's proposed new revisions to simplify guidelines are highly restrictive and would make regulatory relief to challenge unreasonable rates virtually non-existent for all but a few facilities shipping "miniscule" volumes of grain and grain products. But, again, these rules serve rail customers - the grain elevators -rather than my wheat producers. This situation has continued far too long. The STB recently, after listening to years of rail customers' grievances, finally changed its methodology for calculating the cost of capital to Capital Asset Pricing Methodology (CAPM) on the railroad. This could result in benefit to shippers as more railroads will be revenue adequate under the new standards. While these changes are significant, they still fall short of producing a pro-active STB that growers can rely on for relief from captive rates and service.

This frustration with the lack of regulatory oversight has led us to help develop and support legislation that would strengthen the rules of the game for growers. We believe parts of H.R. 2125, the "Railroad Competition and Service Improvement Act of 2007" introduced by Chairman Oberstar, would address some of our concerns regarding both rates and service. This bill would put us in a position to be treated as a customer should be treated. The basic thrust of HR 2125 (companion bill S953) is to restore the provisions and tenants of the Staggers Rail Act of 1980 which provides for fair treatment of captive shippers as the railroads were partially deregulated.

H.R. 2125 contains language addressing areas of inadequate competition, common carrier obligation, bottleneck, terminal access, paper barriers and developing a system of arbitration of rate and service issues, called final offer arbitration that mirrors a system that has and continues to work well in the resolution of rail/shipper disputes in Canada. These are complex subjects for complex problems, in a business where one size does not fit all.

We also support H.R. 1650 (companion bill S. 772), the "Railroad Antitrust Enforcement Act of 2007" introduced by Representative Tammy Baldwin, which would remove several antitrust exemptions for the railroads.

While we support these bills, we also know that these issues will take time to move through the congressional process. So, paying heed to the old axiom "if you are not at the table, then you are on the table", we have begun a process of problem-resolution with one of the four major Class I railroads. The National Corn Growers Association, the American Soybean Association, the National Association of Wheat Growers and other agriculture interests, along with representatives of BNSF Railway, have formed the Ag Rail Business Council. Our first meeting was in February, and I will say we were treated like customers, rather than as a third-party who happens to be picking up the bill for freight.

The agenda included discussion on railcar allocation, harvest congestion, differential pricing, revenue/variable cost ratios, and a discussion on what constitutes a "reasonable freight rate." Some of these topics will require considerable homework on our part, but we are determined to find solutions for our growers. This is a forum to educate the railroad about the needs of producers. It will also enhance our understanding of the rail freight business, with the ultimate goal of finding mutually beneficial solutions.

Conclusion

Madam Chairman and members of the committee, wheat industry leaders have been working on rail rate and service issues for thirty years. We believe the complexity of this issue has been a deterrent for many of the parties involved, including Congress. It would be easy to throw in the towel and say "we're tired", but we can't do that. Ample opportunities exist to increase service to American agriculture, such as new STB accountability, H.R.2125, S953, HR 1650 and S772, and coalitions like the Ag Rail Business Council.

We understand that new railroads are not going to be built, so competition in that sense is unrealistic. What we can accomplish is accountability on all sides, to find good service at reasonable rates.

Madam Chairman, thank you, again, for allowing me to be here today to share our views and provide education on this very important issue. I am ready to answer any questions that you and other committee Members may have.

Many of the specific rail issues are detailed in the October 2006 GAO report on rail competition and capacity. The internet link to this report is: http://www.gao.gov/new.items/d0794.pdf

RAIL COST PRIMER

Railroads rate levels can be evaluated based upon the comparison of the rate level compared to the variable cost associated with the movement. The revenue to variable cost analysis gives the reader a perspective on the relative profitability of the rail movement.

Generally all rail costs are measure in variable costs.

- 100 percent of variable costs - One hundred percent of variable cost is exactly what one would think it means – namely the variable cost associated with a particular movement. Cost that vary with output such as labor, fuel, wear and tear of equipment, etc. Generally, it does not make sense for any business to perform its service for less than the variable cost associated with the service.
- 140 to 150 percent of variable costs – this figure is generally accepted as the level at which the railroads cover all costs and make a decent return.
- 180 percent of variable costs – this is considered the threshold of unreasonableness by the Surface Transportation Board.
- In the various state rail cost analyses, one will find that the captive origins (lack of choice of rail carrier) will have the highest revenue to variable cost levels. In parts of many states where there is no rail competition, one can find rates that are 200-250 percent or event 350 to 400 percent of variable cost. These are extremely high rail rates and show the high degree of captivity of the local rail shippers.

The calculation of rail costs can be somewhat complicated. Whiteside & Associates, Billings, Montana utilizes a rail costing model developed in conjunction with FRN, Inc and the rail costing mirrors revenue to variable cost levels found at the STB.

David Cleavinger
President
National Association of Wheat Growers

David Cleavinger is a fifth-generation Texas farmer and rancher operating his 4,500-acre irrigated family farm and ranch in Wildorado, near Amarillo. His crop production has included wheat, corn, grain sorghum, seed milo, sorghum silage, cotton and sugar beets along with stocker cattle. In 1979, he earned a degree in agriculture business and economics from West Texas A&M University.

David began his leadership in agriculture with the Texas Agriculture Lifetime Leadership (TALL) program in 1992. This two-year program allowed him to study agriculture enterprises and local economies throughout Texas and provided the opportunity for travel to Mexico, Argentina, California and Washington, D.C. David also served as chairman of the Texas Rural Communities Board in Austin, which provides grants and loans to start up businesses in rural Texas.

David has been an advocate for agricultural policy at the state and federal level for more than 15 years. He served as chairman of the Texas Wheat Producers Board in 2000 and represented Texas on NAWG's Domestic Policy Committee during the negotiations of the 2002 Farm Bill. In 1996, he served on the U.S. Wheat Associates Board of Directors and traveled to Europe and the Middle East to promote U.S. wheat products to foreign buyers.

David and his wife, Jackie, attend Hillside Christian Church in Amarillo and have been married for 29 years. Jackie serves as business manager for Wildorado Independent School District, the board of which David has served on in the past. They have two children, Kent, who is in the family farming operation, and Kelly, a sales representative for Graham Data Supplies in Amarillo.

National Grain and Feed Association

1250 Eye St., N.W., Suite 1003, Washington, D.C. 20005-3922, Phone: (202) 289-0873, FAX: (202) 289-5388, Web Site: www.ngfa.org

TESTIMONY by

NATIONAL GRAIN AND FEED ASSOCIATION

Before the

COMMITTEE ON SMALL BUSINESS

U.S. HOUSE OF REPRESENTATIVES

May 1, 2008

Chairwoman Velazquez, Ranking Member Chabot, and members of the committee. I am Kendell W. Keith, president of the National Grain and Feed Association (NGFA). The NGFA has 900 member companies that operate approximately 6,000 plants and facilities that receive grain from farmers for storage, processing, shipping, and marketing throughout the year. The vast majority of our company members are small businesses and the majority of the customer base for our members are small business family farmers. This hearing is very timely, as freight capacity for hauling grain and other agricultural produce has become increasingly constrained in both the rail and other transport sectors.

Grain Marketing and Movement from Farm to the First Buyer

After grain is harvested, farmers may choose to deliver grain to a local livestock feeder, a commercial feed manufacturer, or grain processor; but most grain is delivered first to an elevator that can store the grain and later re-sell the grain to other processors, feeders or exporters. The value of the grain to the farmer is generally established by the grain elevator operator at the time the farmer delivers the grain, and transportation costs play a significant role in determining the price of grain at a given location. The elevator operator surveys alternative end-use markets for the grain, subtracts the cost of freight and an operating margin and the net value is what he bids for the farmers' grain delivered to the elevator. So, while the elevator that ships the grain pays the railroad directly for the cost of freight, in actuality, it is the farmer that ultimately makes the payment for the movement of the grain to a destination market.

Grain Movements from Elevators to End-Users

While farmers generally truck their grain to the first buyer, the grain elevator that stores and ships the grain may use one of three primary modes to reach end-use markets: barge (if the elevator is located on a navigable river system), rail or truck. Of all commercial movements of grain, approximately 1/3 is moved by rail, 1/5 is moved by barge and the remainder is trucked to destination.

Since most elevators are not located on a navigable river, the most typical transportation situation is for a grain elevator to have access to both rail and truck transportation. Generally, rail is used to reach more distant markets (300 miles or farther away) and trucks are often more economic for shorter-distance hauls.

While the elevator may have access to both rail and truck transportation, (with the exception of some terminal markets) it is rare that an elevator will be located at the juncture of two rail lines, a situation that would provide for direct rail-to-rail competition. Thus, for long-distance movements of grain, the elevator is generally dependent on a single railroad. And railroads are fundamentally different than truck and barge transportation. With trucks and barges, the rivers and highways are open to any carrier that wishes to operate; thus competition is readily available. In contrast, railroads own and maintain the rail bed and infrastructure, and generally do not permit other carriers to operate on the right-of-way. This fundamental difference with rail transportation can sometimes create situations where rail competition is restricted and cannot be relied upon to discipline marketplace behavior or pricing of freight service. This is the primary justification for maintaining the Surface Transportation Board and for regulating railroads differently than truck and barge.

Trends in Rail Transportation and Rail Access for U.S. Agriculture

While demand for grain transportation has a significant seasonal component, with the greatest demand typically coming during harvest, overall rail capacity in the U.S. was generally in surplus during most of the 1980s and early 1990s. Even so, the rail share of grain transportation declined sharply since the Staggers Rail Act was passed in 1980. In 1980, railroads carried 50% of the grain that was shipped from elevators. Today that share is about 33%.

But the days of surplus rail capacity are over. In the last 4 years, there are growing signs that the rail industry is nearing its capacity limits, at least in some shipping corridors. The biggest growth sector for the railroads and the factor that has contributed most to the tightening rail capacity has been intermodal freight, much of which is in the form of imports of manufactured goods from Pacific Rim countries.

Physical Access to Rail Service. Rail service to the agricultural sector has been trending toward longer and longer train sizes. A "unit train" is a single train of cars with an identical commodity, loaded at a single origin point and generally unloaded at a single destination. The railroads have been encouraging the grain elevator industry and grain users, such as processors, to build the handling infrastructure to be able to ship longer

trains. Longer trains from a single location are more efficient for railroads, so there is generally a price advantage for such freight. And since farmers ultimately pay for the freight, there is a passback of freight savings to the producer in the form of higher local cash prices. At the same time, the increasing concentration of grain handling at fewer loading points means that there may be fewer rail loaders for farmers to deliver to, causing the average farm-to-market distance to be longer. So, the efficiency gains of rail carriers moving larger trains has the effect of putting added traffic on highways and local road systems. The added cost of highway repairs, of course, is borne by the taxpayer.

Economic Access to Rail Freight. With the tightening rail capacity, not unexpectedly, railroads have been increasing freight rates. Shown in the table below is a comparison of the percentage change in revenue per unit for the last 3 years, comparing agriculture to other categories of freight. For the U.S.-based carriers (Norfolk Southern and CSX in the Eastern U.S.; and Union Pacific and Burlington Northern Santa Fe in the Western U.S.), agricultural revenue per car is up between 27 and 52% (simple average of 43% across all carriers). And in most cases, the percentage change in freight charges are higher for agricultural shippers than for all railcars. (The BNSF is the one exception to this pricing pattern.)

Does this indicate that agricultural shippers are being treated unfairly, or that railroads have more pricing power with agricultural shippers? Not necessarily. As the percentage of total rail movements in the intermodal sector grows, the average revenue increase per unit across the entire railroad tends to be dampened because the revenue per unit for intermodal is typically lower than for other types of shipments. (It should be noted that in the case of intermodal shipments, a single intermodal car may carry between 2 and 4 units.) While one cannot conclude with certainty that agricultural shippers are incurring generally higher rate increases from rail carriers compared with other rail customers, it is a situation that should be monitored over a period of years to see if current trends continue.

3-year Change in Rail Revenue per Unit

(1st QTR 2005 to 1st QTR 2008)

U.S. Railroads	Agriculture	Coal	Intermodal	Total
Norfolk Southern	49%	40%	17%	30%
CSX	45%	48%	10%	38%
Union Pacific	52%	27%	24%	33%
BNSF*	27%	29%	34%	32%

*BNSF data compare 1st Qtr 2005 to 4th Qtr 2007, because 1st Qtr 2008 BNSF data was not available at the time of this writing.

If a rail freight rate is excessive, are there solutions available? Generally, challenging rail rates before the Surface Transportation Board is a very costly exercise. The STB attempted to make rate challenges for smaller rate cases easier and less costly when it

issued its decision on "Ex Parte 646" in September 2007. There are three cases now pending under those revised guidelines before the STB that should be completed in July of this year. Those cases may help determine how practical these new STB rate case rules are for rail customers. Regardless of the outcome of those particular cases, NGFA estimates that challenging rates on agricultural shipments will still cost about $250,000 per case, and the STB has placed a cap of $1 million on maximum rate relief that can be obtained under the so-called "3-Benchmark" simplified standard. In our comments to the STB in this rulemaking, as well as subsequently, the NGFA has told the agency that this cap is much too low and effectively will put many potential rate cases out of reach economically. (Note that this STB ruling is now being challenged by the Association of American Railroads and several Class I railroads in the DC Circuit Court of Appeals.)

Even if the rules can be changed to give greater access to rate relief for small shipments, we do not believe that rail rate challenges before the STB would ever become a popular course of action for rail customers, because litigation with a carrier that they are so dependent upon risks souring a business relationship that may be critical to business survival. But we do think it's important to have access to reasonable litigated solutions so that rail carriers are encouraged to negotiate rate resolution with customers. To promote business-to-business negotiation, the STB needs to make the rules as practical as possible. Lowering the bar to rate challenges is important to a healthy business environment for rail transportation.

Pending Rail Legislation

H.R.2116 would amend the Internal Revenue Code to allow tax credits for 25% of the cost of new qualified freight rail infrastructure property. While railroads already are re-investing some of their increasing profits into expanded infrastructure, we think that legislation like this bill could encourage higher levels and more rapid investment to take place. NGFA intends to support this legislation with some minor changes to be recommended to ensure that the tax credits are available to rail customers that also invest in rail infrastructure that can help reduce congestion on railroads and contribute to overall rail capacity.

H.R.1650 would remove the railroads' antitrust exemption and give the STB six months to review proceedings to bring the railroads into compliance with antitrust laws. The bill would further give the U.S. Attorney General, state attorneys general and private persons the ability to file suit in federal district court to challenge railroad actions on antitrust grounds. While NGFA is attracted to the fundamental logic of this bill, i.e. that railroads should be required to "play by the same rules" as all other businesses, we are not certain of the practical value of the bill. How much would market discipline be affected by the passage and implementation of such bill?

There may be other forms of rail regulatory reform that could also be helpful. For example, we would like to see the "national rail transportation policy" amended to direct the STB to strike a more reasonable balance between protecting rail revenue for carriers and protecting the business needs of rail customers. Current policy is more heavily

skewed to the former. We think that legislation might also be considered to modify railroad "revenue adequacy" provisions to more realistically reflect the cost of capital. (Note that the STB recently took action on this matter and adopted a standard that is an improvement. However, now the agency appears to be in the process of reconsidering that decision.) NGFA would also be supportive of a change in the statute to address unnecessary delays in issuing decisions. (A recent decision by the STB required five years from the date of original complaint until a decision was issued. It does appear that in some recent proceedings, the STB is making an effort to expedite the process somewhat, but extended litigation in proceedings is very discouraging to rail customers that otherwise might make use of the protections intended to be afforded them under the law.) Lastly, if the STB fails to ultimately adopt workable rules for challenging small rate cases, we believe that Congress should pass legislation directing the STB with great specificity as to what such rules should be. We don't think that practical rules for challenging rates will promote litigation; we think such rules will promote healthy business relations between carriers and their customers.

Thank you for the opportunity to testify and I look forward to responding to any questions you may have.

National Rural Electric
Cooperative Association
A Touchstone Energy Cooperative

4301 Wilson Boulevard
Arlington, VA 22203-1860
Telephone: (703) 907-5500
www.nreca.coop

BEFORE THE

U.S. House of Representatives Committee on Small Business

Rail Transportation Access for Small Businesses and Family Farmers

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TESTIMONY OF

Nelle P. Hotchkiss
Senior Vice President of Corporate Relations
North Carolina Electric Membership Corporation

Thursday, May 1, 2008
10:00 a.m.
1539 Longworth House Office Building

Madame Chairwoman and Members of the Committee:

My name is Nelle Hotchkiss and I am the Senior Vice President of Corporate Relations for the North Carolina Electric Membership Corporation (NCEMC) and the North Carolina Association of Electric Cooperatives (NCAEC). Our membership consists of 26 electric cooperatives serving over 2.5 million consumers in 93 counties in North Carolina. I appreciate the opportunity to speak before you today about the issue of rail transportation and the importance of adequate rail competition in my state and across this nation.

As member-owned, not-for-profit organizations the obligation of rural electric cooperatives is to provide a reliable supply of electricity to all consumers in our service areas at affordable rates. We take our obligation to serve very seriously – the personal and economic health of our members, our communities, and our nation depends on it.

Our National Rail Policy is Broken

Electric Cooperatives are dependent on the railroads for the transportation and delivery of coal. Simply put, we do not believe that America's four major railroads are meeting our transportation needs in the most efficient and dependable manner. Electric cooperatives and other rail customers do not receive reliable rail service at reasonable rates. The Surface Transportation Board (STB), the government agency charged with the regulatory responsibility of for the nation's railroads, is not addressing crucial rail customer rate and service problems.

Some utilities are being forced to buy more expensive foreign coal because they can't rely on railroad deliveries from the Powder River Basin – the richest source of low sulfur coal in the world.

Electric cooperative consumers in North Carolina and around the country have experienced deteriorating rail service and sharply increased rates. For example, from 2002 to 2007, North Carolina's electric cooperatives experienced a 45% increase in the coal freight component of our energy cost which, in turn, was reflected in the wholesale rate for power. That increase calculates to over $8.7 million dollars in higher costs during this time frame that have been borne by our end consumers; residents, small farmers and small businesses. Service problems and high rail costs occur primarily in areas where shippers are captive – meaning they have no transportation option but to use a single railroad.

The Captive Rail Customer

Captive rail customers are shippers who must rely on a single railroad to deliver their products. These customers usually move bulk commodities such as coal, grain or lumber, or certain materials that, due to size or characteristics, cannot be moved on our nation's highways.

Historically, 20-30 percent of the nation's rail movements have been "captive," with many of these movements covering rural America. Today, in a capacity-constrained rail system, a majority of rail movements may lack competition.

Captive Shippers Suffer Monopoly Abuse

The nation's antitrust laws are meant to protect consumers and the overall public interest from anti-competitive behavior by businesses. The railroads are exempt from antitrust laws and do not play by the same rules. The railroads' antitrust exemptions are antiquated, have no public policy justification, and allow anticompetitive conduct. The resulting lack of competition, together with the ineffectiveness of the STB, have allowed

freight railroads to reap huge profits – with no marketplace consequences or legal accountability for their unreliable service and exorbitant rates and fees.

How Did We Get Here

Since the mid-20th century, freight railroads have been exempt from the nation's antitrust laws; but, until 1980 they were subject to tight regulation by the Interstate Commerce Commission. By the late 1970s, the industry was in poor financial condition with an excess of capacity. In an effort to revive the rail industry, Congress in 1980 deregulated competitive rail service and allowed the railroads to shed their excess capacity. Railroads were free to shed marginal routes and enter into long-term shipping contracts.

Unfortunately, in 1980, Congress failed to remove the industry's antitrust exemptions.

The intent of the legislators was to replace government regulation of the railroads with market competition, while ensuring that those rail customers without access to transportation competition receive reliable rail transportation at reasonable rates.

Unfortunately, today, rail customers:

- Lack access to competitive rail transportation;
- Lack access to a fair and workable process for challenging rail rates for movements that lack access to competition;
- Are paying steeply higher rail rates while suffering unreliable rail transportation;
- Are without adequate remedies for unreliable rail transportation; and
- Are concerned about the ability of the rail industry to provide both current and future transportation needs.

Without abandoning the 1980 deregulation of competitive rail activities, a refined and improved national rail policy for the twenty-first century is needed to ensure effective rail transportation competition, protect "captive" rail customers from monopoly abuse and ensure the reliable delivery of the nation's freight at reasonable rates.

Why Captive Rail Is A Problem

With no competitive options, no antitrust protection, and a passive STB that is failing to provide effective oversight, freight rail customers face unrestrained shipping costs and unreliable service. The resulting cost increases are passed on to consumers who buy their products and use their services.

While the major railroad companies log record profits and stock prices on Wall Street, delays in coal deliveries have caused higher electricity prices on Main Street. Skyrocketing transportation costs are forcing chemical and paper companies to consider moving American jobs overseas. Already a handful of utilities are importing coal from Columbia and Indonesia in order to meet consumer demand because the railroads are not delivering adequate supplies of U.S. coal.

U.S. taxpayers helped build the rail routes and the companies that operate them. A reliable and reasonably priced freight rail system is critical to the American economy and infrastructure. While railroads are enjoying record profits, rail customers are paying more and getting less.

The end result is unreliable rail transportation, unreasonably high rail rates, concerns about inadequate rail capacity, and concerns about whether the nation's major railroads have the ability, both now and in the future, to serve the nation's transportation needs. In the end, it is consumers that must pay the price for the inadequacies of the current rail system.

Rail Competition Issues

In 1980, Congress adopted legislation to replace government regulation with market competition. This, of course, only works if there is competition. (This entire

debate concerns those rail customers who cannot use any other mode of transportation; those that can use trucks or barges have long ago escaped rail captivity via those routes.) Despite the rhetoric of the railroad industry, the current debate is only about how partial railroad deregulation is working for "captive rail customers" – those without access to competition.

Currently, 20 percent of all rail traffic is captive. The best way to reduce this percentage is to increase access to competition. Since the notion of building an entire new rail system is out of the question, the only means to increase access to rail competition is to remove the artificial barriers to competition. No one knows how much the universe of captives will decrease if these competition issues are addressed, but at least some will escape captivity and be governed by market conditions.

Legislative "Reform" is not Railroad "Re-regulation"

The STB is not meeting its regulatory responsibility to balance the needs of rail shippers and the public interest against the monopoly power of the railroads. Over the years, STB decisions and interpretations have actually increased the monopoly power and anti-competitive practices of the nation's railroads. Only the Congress can ensure proper accountability by reforming the sole agency that oversees the railroads.

Two Solutions: Restore Antitrust Laws to Railroads and Strengthen the STB

The railroads must be covered by the nation's antitrust laws just like other industries, and the STB must be more responsive to the public interest and concerns of rail customers. Legislative activity in the 110th Congress has moved to give America the railroad system it needs for the 21st Century, and to correct current railroad abuses. Specific suggestions include the following:

First: Restore Antitrust Laws to the Railroads – Stop Anti-competitive Abuse

Electric Cooperatives support legislation (S. 772, H.R. 1650) that:

- Repeals the railroad exemptions from the antitrust and transportation statutes, so that antitrust law fully covers railroads like other industries.
- Permits the Justice Department and the Federal Trade Commission to review rail mergers under antitrust law.
- Allows state Attorneys General and private parties to sue to halt anticompetitive conduct not currently permitted under rail exemptions.

The Senate Judiciary Committee unanimously voted to pass S.772 out of committee. It was the first time that a congressional panel had sided with shippers over the railroads in nearly 30 years.

Second: Reform the Surface Transportation Board – Make It Perform

Electric Cooperatives support legislation (S. 953, H.R. 2125) that:

- Reverses anticompetitive STB rulings and requires pro-active procedures and pro-competitive policies.
- Installs the same rate challenge process at the STB that other agencies use to protect the public interest and oversee industries with limited competition.
- Creates a pro-active STB that will suspend and investigate unreasonable rail practices.
- Makes the railroad "obligation-to-serve" shippers and the public interest clear in law, with the STB empowered and directed to enforce that legal obligation.
- Lowers STB filing fees to bring these (costs?)in line with filing fees in U.S. District Court.

Conclusion

Madame Chairwoman, thank you for conducting this hearing today. We look forward to working with this committee and with all of the other stakeholders involved to resolve these critical rail transportation issues in an objective and constructive manner.

AGRICULTURAL
RETAILERS
ASSOCIATION

TESTIMONY OF

DAN WEBER

VICE PRESIDENT OF AGRONOMY

CERES SOLUTIONS, LLP

REPRESENTING

THE AGRICULTURAL RETAILERS ASSOCIATION

AT A HEARING OF THE

HOUSE COMMITTEE ON SMALL BUSINESS

ON

"RAIL TRANSPORTATION ACCESS FOR SMALL BUSINESS AND FAMILY FARMERS"

MAY 1, 2008

ARA: Suppliers to America's Farmers
1156 15th Street, NW, Suite 302
Washington, D.C. 20005
Phone # (202) 457-0825
Fax # (202) 457-0864
www.aradc.org

INTRODUCTION
I would like to thank Chairwoman Velázquez for holding this important hearing today. My name is Dan Weber, Vice President of Agronomy, with Ceres Solutions, LLP, a cooperative selling crop inputs and application services in the State of Indiana. I am also Chairman of the Board of Directors at the Agricultural Retailers Association (ARA), which represents a significant majority of the nation's retail dealers who provide essential agricultural pesticides, fertilizer, seed and other agronomic services to America's farmers. As the only national organization exclusively representing the interests of the agricultural retail and distribution industry, ARA is vitally interested in any federal laws or regulations related to the railroad transportation of agricultural inputs utilized in the nation's agricultural sector. As such, I am here today to testify on behalf of ARA. I appreciate the opportunity to discuss this important issue before the Committee.

Ceres Solutions is an agricultural cooperative operating 26 agronomy retail locations (some with rail service) serving 5,000 agricultural producers in 13 Western Indiana and surrounding counties with crop inputs and application services. Total agronomy sales exceed 150 million dollars annually. I began this role in the agronomy division of Ceres Solutions in February 2007, when the coop partnership between Growers, Westland and Agrokey cooperatives was formed. These three cooperatives have each been in business for at least 78 years, and they have worked with the railroads over many decades. Prior to partnership formation, I served as CEO of Growers Cooperative for 6 years. My background includes more than 34 years in agriculture retail sales and management, wholesale fertilizer, crop chemicals and seed distribution in the Midwest Region. In my position as Vice President of Agronomy, I oversee the procurement and receipt of over 125,000 tons of fertilizer with 40,000 tons of that being rail delivered to our facilities. I grew up on a farm in Snake Run Indiana. I graduated from Purdue University with a Bachelor's of Science in Agribusiness Management in 1970. In 1974, following my tour in the Navy, I began working in the agricultural retail industry as a retail agronomy plant manager.

IMPORTANCE OF FERTILIZER & OTHER CROP INPUT MATERIALS TO THE AGRICULTURAL INDUSTRY
Fertilizer use is essential to America's food security and economy. Fertilizer allows domestic farmers to feed and clothe the nation. For every additional dollar of income, consumers in Egypt, Indonesia, and Vietnam spend more than 25 cents on food, while consumers in the United States spend less than 10 cents.[1] We are the best at what we do when it comes to crop production due to newly adapted technology and better understanding and application of sound agronomic practices.

The use of fertilizer is also needed in order to produce enough agricultural products for renewable energy. Renewable energy allows the U.S. to be less reliant on foreign sources of energy. The call went out to the farmers in the United States asking them to produce more corn in an effort to replace part of the dependence on imported oil. They responded by planting a record 92.9 million acres, an increase of 11 percent over the previous year.[2] The world demand for fertilizer to produce more crops for food or fuel is pushing our fertilizer production and distribution systems to their limits.

The three major fertilizer materials we provide our customers are nitrogen (N), phosphates (P2O5), and potassium (K20). Farmers are offered three choices of nitrogen in our market- urea, UAN, and anhydrous

[1] "U.S. Trade Growth: A New Beginning or a Repeat of the Past?" *Amber Waves*, September 2007, available at: http://www.ers.usda.gov/AmberWaves/September07/Features/USTrade.htm.
[2] "U.S. Farmers Plant Largest Corn Crop in 63 Years", National Agriculture Statistics Service, June 29, 2007, available at: http://www.nass.usda.gov/Newsroom/2007/06_29_2007.asp.

ammonia. Urea is a 46 percent nitrogen dry product that we blend with other fertilizer and apply on crops like corn and wheat which use nitrogen. The liquid form, called UAN, is formulated in a solution of 32 percent or 28 percent nitrogen, and anhydrous ammonia (NH_3) is 82 percent nitrogen. Anhydrous ammonia is a pressurized gas in liquid form that requires special handling. Anhydrous ammonia provides the lowest cost to the farmer on a per unit of nitrogen basis making it the preferred choice of nitrogen for many of our farmers. The savings can be $30 to $40 per acre for 175 units of nitrogen on a typical corn crop. Anhydrous ammonia is the most widely used form of nitrogen fertilizer in the Corn Belt.[3] While U.S. corn production has increased, domestic ammonia production has actually declined by 44 percent between 2000 and 2006. During the same period, the number of U.S. ammonia plants declined from 40 to 25 and domestic production capacity declined from 20 million tons to 13 million tons. This decline in production is partially due to rising natural gas prices in the U.S. As such, the market has responded with a 35 percent increase in imports- principally from the Trinidad and Tobago Republic, Ukraine, Russia and Canada.[4] The imported anhydrous ammonia must travel across the country to the corn producing states.

The phosphate offered to our growers is mostly diamonium phosphate (DAP) which is a dry material mined in Florida. It is usually applied with urea and/or potash and is used on all crops. Potassium (potash) is a dry material mined in Canada or imported from Russia and is used on all crops. It is applied straight or blended with Urea and/or DAP.

As an agricultural retailer providing product and application service, our average tonnage moved through one of our retail operation is about 5000 tons of products. We turn our storage about four times in a typical year. In order to accomplish this efficiency, it requires continued timely receiving of products. Product is delivered through the fertilizer distribution network by truck (25 ton per truck) or train (100 tons per car), and both must be timely. Due to the nature of agriculture in Indiana, our crops are very seasonal and with a very narrow window of time for crop inputs to be applied. In the typical U.S. spring, the corn crop will be planted between April 15 and May 20. The grower typically begins to see a yield decrease if planting is delayed past this window. During the fall season, phosphates and potassium are applied to crops. The window of time for application is a little broader in the fall, but the coming of winter weather makes it impossible to cross the fields; thus, putting a certain urgency in the fall fertilizer season as well. This need for the farmer to have his nitrogen, phosphate, and potassium fertilizers on time is one reason that it is so critical that product is in place at our facilities on time. Likewise, it is just as imperative that we receive timely distribution from the truck terminals or railroad service.

There are no substitutes for nitrogen, phosphate, and potassium fertilizers to America's Farmers. These fertilizers must be applied annually to maximize yield production. The challenge that we have in the truck distribution of these nitrogen, phosphate, and potassium products from the terminals is the narrow spring window to plant the corn crop. The typical corn crop in Indiana is planted in a period of two weeks or less due to the size of equipment the farmer has today. The agriculture industry continues to experience consolidations of fertilizer wholesale facilities providing fewer choices to source product and more distance and time required to transport from the terminal to the retail plant operation. Due to the fewer fertilizer producing facilities, rising

[3] "Soil Ph Effects on Nitrification of Fall-Applied Anhydrous Ammonia", Soil Sci. Soc. Am. J. 68:545-551 (2004), available at http://soil.scijournals.org/cgi/content/full/68/2/545.
[4] "Will Anhydrous Ammonium Tip the Balance in the Battle for Acres?", *AgricultureOnline*, September 20, 2007, available at: http://www.agriculture.com/ag/story.jhtml?storyid=/templatedata/ag/story/data/1195585018809.xml.

natural gas prices, and rising transportation costs, the cost of fertilizer to the farmer for anhydrous ammonia has nearly doubled in many places over the past year.[5]

OVERVIEW OF RAILROAD ISSUES

Agricultural retailers use the railroad to transport crop input materials because there is no practical or "reasonable" alternative available. The railroad is the safest, most secure, and most efficient way to move these chemicals. The rail service to our agricultural retail operations plays a critical role in providing distribution due to the large volume of product, the distance it must travel to get to our agricultural retail location, and the restricted seasonal time frame this has to happen. Nearly all the regional fertilizer warehouses are filled by train or river barges. Railroads have claimed that they are at capacity; however, the railroad has failed to submit proof of its alleged capacity while outside studies suggest that the railroad is at capacity in only three percent of its rail area.

Another means of shipping agricultural ammonia is pipeline use. However, existing pipeline are at capacity with two million tons being transported through it. Furthermore, pipelines are not a reasonable alternative to many of our rural markets because there is limited access to the pipeline. In addition, in our market area, the distribution of anhydrous ammonia through the pipeline system is taxed to the maximum in part due to the seasonal demand and also the decrease in anhydrous ammonia storage along the pipe. For example, at the Crawfordsville Koch location, 64,000 ton of storage at the pipe terminal was scrapped due to concerns over the integrity of the storage tanks. The storage was not replaced; thus, putting more pressure on the anhydrous ammonia distribution system.

There are not enough trucks or qualified drivers to distribute the tons currently moved by rail cars in the time required for it to be used in agriculture. The trucking industry already has strained capacity. According to the American Trucking Industry, the trucking industry is currently short 20,000 drivers and that deficiency is expected to increase to 80,000 drivers by 2011. Furthermore, with new Department of Transportation regulations in place, it is much more difficult to find trucks to haul anhydrous ammonia then it was 5 years ago. There are fewer drivers that have the required commercial driver's license with a HAZMAT endorsement than we had pulling anhydrous ammonia tanks prior to the new rules. Almost a third fewer qualified truck drivers to service our industry and more demand on their service as we lose rail delivered anhydrous ammonia service. Even if there were enough certified truck drivers to handle the additional freight, the idea of transporting the material by truck rather than rail flies in the face of the goal to lower carbon emissions that the U.S. is working hard to achieve.

The cost of rail service to our agricultural retail operations has increased at a rate that forces us to look at alternatives but finding few. We require a greater gross margin to cover these increased operational costs which pushes the farmers to need more for the crops they are providing for food. For example, dry rail fertilizer tariffs into Indianapolis increased from $33.32 per ton for a single car shipment of DAP out of Florida in July 2005 to today's rate of $52.63 per ton. That is an increase of 58 percent in three years. Another example is the cost of anhydrous ammonia rail shipments out of Tampa, where the imports arrive. The cost of rail service was $22.79 per ton from Tampa, Florida to our facility at Rensselaer, Indiana in 2000. Today's rate is $163.55 per ton, thereby eliminating the opportunity to source imported lower cost anhydrous ammonia out of Tampa. Every time we switch from using a rail car to trucking the same volume of material, we put four more semi tractors pulling 25 ton loads on our all ready crowded roads further distances. We use more fuel, create more lines at the truck terminals decreasing our efficiency and increasing costs as trucks sit in those lines and we expose the

[5] "Dealer Report Regional Prices", *Green Markets Dealer Report*, Vol. 22, Number 17, p. 4.

public to four times the exposure as the truck go though our cites and small towns. There is also a greater security threat when the chemicals travel by truck rather than train.

EXAMPLES OF HARMFUL PRACTICES & DETERIORATION OF SERVICE
For the preceding reasons, agricultural retailers and farmers must continue to use the railroad system for transportation of agricultural inputs despite the railroads' continued abuse of shippers.

<u>ABANDONMENT OF SERVICE</u>
The railroad has continued to decline in timely service by the rail in placement of cars being held in yards for distribution. I have been in the agricultural retail business for 34 years, and I've witnessed a decline in the service and increase in cost for much of my career. In the 60's the industry moved from an animal manure and bagged fertilizer placed in the crop plant row to using bulk fertilizer and broadcast application. These new bulk fertilizer agricultural retail facilities were built next to railroads to take advantage of the efficiency and volume rail cars provided. In the 70's we still had most of our agricultural retail outlets served by rail with acceptable service being provided. In the 80's we saw the beginning of the abandonment of many of our rail lines to our smaller communities and business operations. By the 90's we lost most of our rail service to smaller communities thereby increasing the costs of these operations which triggered a consolidation in retail facilities.

<u>FUEL SURCHARGE</u>
The rail tariff increases and fuel surcharges experienced in past 3 years are also examples of unreasonable and excessive fees. The railroad's surcharge on fuel was 10.8 percent in 2005. It increased to 16.0 percent in December of 2006 till it moved to 26.8 percent in November of 2006. The surcharge decreased to 14.8 percent in 2007 and in 2008, the railroad began to use a "factor" that makes it difficult to compute what percentage increase it reflects. The somewhat hidden surcharges added to the tariff are the "Seasonal Price Factor". In 2005 it was $350 per car. In March of 2006 it was $200 per car plus there was "Equipment Surcharge" added $550 per car through the fall season. In April of 2006 this was reduced to $250 per car. The railroads use this illusive pricing scheme only because they can, and because there is little oversight and no competition. The STB has made an effort to address this issue, but the problem with transparency continues to exist.

<u>CONNECTOR FEE</u>
Another example of excessive fees is the railroads' practice of arbitrarily invoicing for services. For example, I am charged $6,000 per year for the "Annual Sidetrack Connection Charge." I later received a letter from the railroad stating that if we did not receive a minimum of 25 carloads of freight per year, we would have to pay an "annual sidetrack connection charge" of $6,000. Most of our smaller agricultural retail outlets receive four to six cars annually. Enforcement of this policy would prohibit most small agricultural retail outlets from being able to receive shipments as it would not let them be competitive with the additional costs passed on to their retail prices.

<u>LOSS OF SERVICE</u>
Next, the railroad's failure to respond to the needs of America's agriculture industry and rural communities by abandoning of rail service to agricultural retail locations that are not unit train receivers. The railroads defend their action by stating that it is much more economical to service the 65 or 85 car houses. The railroad's price increase on phosphate shipments out of Florida is a prime example of the railroad's preferential treatment to unit train shipping. On June 1, 2008, the single car rate will increase by 10 percent, while unit train shipments of 65 to 84 cars will increase 6 percent, and unit train shipments of 85 or more cars will increase only 3 percent. As a small agricultural retailer, I do not make as much money when I custom apply fertilizer on the 10 acre field

as I do when I apply fertilizer to the 100 acre field, but I do it. I do it because I have competition. If I were a monopoly, I would tell the 10 acre farmer he would have to merge with his neighbor and get bigger before I would waste my time providing a service, but I am not a monopoly, nor do I care to conduct business as one.

The railroads behave in this manner because they know that they can when there are only four major railroads serving different geographical regions of the country.

TARIFFS

The railroads neglect the needs of the agricultural industry by abandoning tariffs systems in which the dealers considered when they made long-term investment decisions. The railroads arbitrarily change their tariff structure without giving the industry warning. In 2001, we purchased a fertilizer warehouse and distribution facility. One of the things that made it attractive and economically doable was the advantage gained because the facility had a reduced rail tariff based off its ability to receive 15 car units of fertilizer at a time. This was an advantage until a couple of years ago the discounted tariff was raised to 65 cars, leaving the facility at the single car tariff rate. There were no indications this would happen when we visited with them regarding the 15 car tariff at the time of the acquisition. It was and is a severe economic hit to this operation. The railroads make it difficult for businesses to invest in operations because the businesses do not know when the railroads will change the tariff system, thereby decreasing the investment value and increasing the costs of operation.

FAILURE TO MEET CONDITIONS

The railroads harm the small business owner by failing to meet expressed conditions made by themselves to shippers. I recently visited with managers at another cooperative in the Midwest about the problems that they have experienced in doing business with the railroad. Three years ago, the cooperative was expanding by building a new 35,000 ton dry hub plant. To use the new plant, the cooperative needed to add almost a mile of track siding with two switches which are required by the railroad, one switch to the north and one to the south end. The railroad and the cooperative negotiated a deal to help offset the $1.5 million cost of laying the rail by the plant. These negotiations continued for a year. The railroad promised the cooperative credits for cars received. The railroad negotiator gave the cooperative a verbal confirmation that there would be car credits, but failed to put the deal in writing. Before the agreement was approved by railroad management, the railroad's negotiator retired. The cooperative had already invested in the plant and built the track during this year long negotiation process, relying on the railroad's promise that there would be tax credits. In the end, railroad management turned down the proposal, leaving the cooperative with no credits to offset the costs of the rail siding built and no recourse. This is another example of how the railroad's failure to do business honestly abuses the agricultural industry, abuses the small business owner, and stifles investment in the U.S.

RATE CHANGES

An additional example of a failed railroad system is that there is no recourse for the small business operation to challenge the rail decisions. There appears to be little recourse if a shipper suffers due to the railroad's failure to deliver product on time, while the shipper suffers because his customer goes elsewhere for the product. We have experienced many delays in placement of cars this spring causing economic hardship, additional freight costs, and potentially carryover of this inventory showing up late into the next crop season. I have been told that the legal cost to arbitrate with the railroad is in the hundreds of thousands of dollars and can take several years.

NEW COSTS FROM FEDERAL SECURITY RULES

I was recently told that due to the new Department of Homeland Security rules prohibiting storing anhydrous ammonia in the rail yard over 48 hours, we would have to either receive the car (this was not an option due to the rain causing a delay in our farmers use of the product); return it to the shipper (not a good option as the product is somewhat allocated), or I would have to have it placed on one of our other side tracks. We had room at another facility five miles from the rail yard, so the railroad took the cars to the other facility. Following the rail company moving the two cars of anhydrous ammonia, we received an invoice for $52.85 per ton. There are 80 tons in a railcar, making the total bill $8,456. After several calls pleading my case for thinking this was somewhat excessive, I received help in a reduction of the bill to $8.75 per ton or a total of $1,404. When our customers were ready to use the anhydrous ammonia because the weather improved, we asked the railroad to move the two anhydrous ammonia cars to the original destination. After moving the two cars five miles, I again received an invoice for the originally charged rate of $52.85 per ton. I have not started the process of trying to get this rate reduced at this time; however, if there were competition, this type of pricing would not be a competitive bid for this rail service.

INHERENTLY SAFER TECHNOLOGIES ARGUMENT

In the aftermath of September 11th, for safety and security reasons, Federal regulators began issuing new rules that apply to agricultural retailers and the chemicals that they store and apply. Congress and Federal regulators are currently considering a law that would mandate America's agricultural industry to use inherently safer technologies (IST). ISTs include input substitution, catalyst or carrier substitution, process redesign, product reformation, procedure simplification, and technology modification. The agricultural retail industry is already heavily regulated for environmental and security reasons; thus, ARA believes that mandating IST regulations would be excessive.

Ammonia and chlorine are the two most common toxic-by-inhalation (TIH) chemicals, of which ammonia is used extensively in the agricultural industry. The railroads have made it clear that they do not want to transport TIH chemicals. Much of the aggressive behavior mentioned previously is attributed to the railroad's reluctance to carry ammonia and other TIH chemicals. The railroad argues that the agricultural industry should use ISTs in place of the TIH chemicals currently used.

There are several problems with the railroad's argument for IST. First, there is no excess fertilizer production in the current global market. Fertilizer is being produced and used at a ratio of one to one, which means that it is not possible to switch from one type of fertilizer to another type. Even if substitution of fertilizer were possible, if the reports that the railroad is at capacity are true, the railroad does not have the capacity to carry the larger quantities of alternative fertilizer required to match the potency of anhydrous ammonia. Second, there is no alternative input chemical for ammonia. The railroads claim that there is an alternative, but they have not shared their research with the rest of the agricultural industry. If there were a viable economical alternative, the agricultural industry would likely welcome its use given the shortage of fertilizer that we currently have.

Under the Stagger Act, the railroad is to function as a "common carrier" in exchange for the government's original substitutes, financial bailouts and protection. As a "common carrier", the railroad is responsible for carrying all of the nation's goods- not just the ones that the railroad would prefer to carry. The Surface Transportation Board (STB) defines the common carrier obligation as the, "duty of railroads to provide transportation or service on reasonable request."[6] The STB attempts to create a loophole for the railroads by

[6] "Railroad Shipping: STB to Hold April Meeting on 'Common Carrier Obligation' of Railroads, *Logistics Management*, February 2, 2008, available at: http://www.logisticsmgmt.com/article/CA6535371.html.

debating the word "reasonable". However, transporting fertilizer must be deemed a "reasonable request" when the very same law that the STB Chairman references to defend the railroad's unwillingness to fulfill its obligation explicitly lists the railroad's responsibility when transporting "agricultural products, including grain and fertilizer."[7] The STB's authority does not trump the laws made by Congress nor does the STB have the authority to interpret and change laws. The STB is an economic regulatory agency that Congress created to resolve railroad rate and service disputes and reviewing proposed railroad mergers.

RECOMMENDATIONS

ARA has several recommendations for improving railroad service to the agricultural sector.

REFORMING THE STB

First, ARA supports reforming the STB to make it more accountable and responsive to shippers. The railroads' arbitrary taxing on cost and raising the tariffs, indicates that there is no oversight of the railroads' actions. The STB appears to have no interest in our issues as small business operators. Why would the STB continue to allow the railroads to eliminate service to our rail houses and push towards unit train receivers only if they truly had the public best interest in mind?

USDA RAIL STUDY

Second, ARA supports the proposed United States Department of Agriculture (USDA) rail study of the impact of the railroad on the agriculture industry. The proposed provision is up for consideration in the Farm Bill debate. This study would provide more information to legislators and small business owners in the agricultural industry. The study would also result in more transparency between the railroads', its customers, and lawmakers.

TRANSPARENCY IN CHARGES AND RATES

Third, ARA believes that there should be more transparency in fuel charges and rates. It is impossible for the occasional or seasonal shipper to compute the fuel surcharge, and too expensive for a small business to go to STB to challenge rate. The railroads take advantage of this power imbalance and confusing rate structure by behaving like a monopoly. For example, Ceres Solutions sells the rail company about 250,000 gallons of fuel for their locomotives. We fill them at night or on the weekend- whenever they call. We asked about having the railroad pay us a fuel surcharge for the truck that has to service their train, they refused and said they would get someone else to do it before they would pay us a surcharge. Transparency in the fuel charges would encourage competition and discourage this monopolistic-type of behavior.

RAIL CAR REDESIGN

Forth, ARA encourages further research to be conducted in order to determine whether the railroad's proposed new rail car design is an effective design. The railroad and the Department of Transportation are considering designing a new rail car which is heavier than the currently used cars. There is evidence that the new car would be too heavy for some of the current railroad tracks to support when filled with some agricultural inputs. The railroads should not invest in new cars that further limit their service, and they should design a car that can continued to be used on the current track since it is rarely upgraded.

COMMON CARRIER OBLIGATION

Fifth, ARA thinks that the railroads' common carrier obligation should be maintained. Since 1980, the railroad industry has shrunk from 40 lines to four major lines because of the government's protection of the industry. If

[7] 49 U.S.C.A. § 11101 (a) (d) (1988).

the government is going to protect the industry, the rail industry should serve all of the U.S. in return. The railroad has the duty by law to be the common carrier; their performance of that duty should not be left to the railroad's discretion.

REVIEW OF THE ANTI-TRUST EXEMPTION

ARA recommends Congress review H.R.1650, which would remove the railroads' antitrust exemption and give the STB six months to review proceedings to bring the railroads into compliance with antitrust laws. It is our understanding that this legislation could help bring competition and fairness to the railroad industry.

CONCLUSION

ARA and our members strongly support a railroad system which is healthy financially, but we believe it is important to have a railroad infrastructure that is not needlessly sheltered from competition and left to operate without proper oversight. America's agricultural industry is currently faced with high fuel, fertilizer and transportation costs. If the railroad is left to operate in its current environment, the agricultural industry may be stalled in its productive capacity, and the U.S. will continue to see food and energy prices soar. The current railroad regulatory environment may help further drive many within agriculture out of business and increase our dependence on foreign sources of food and fiber.

Thank you for considering ARA's views. We appreciate Congresswoman Velázquez interest and support on this important issue. We welcome the opportunity to provide further input to the committee on the issue of the rail transport of agricultural inputs. ARA stands ready to work with Congress on the development of railroad legislation that adequately reflects the needs of America's agricultural industry and our rural economy. As we face these challenges, we can only accomplish what needs to be done if we work together.

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